Constructing continuity in economic ideas in the IMF

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Abbreviations

AFC	Asian Financial Crisis
BIS	Bank for International Settlements
BWS	Bretton Woods System
FAD	Fiscal Affairs Department
FSAP	Financial Sector Assessment Programme
FSB	Financial Stability Board
FSF	Financial Stability Forum
GFSR	Global Financial Stability Report
GDP	Gross Domestic Product
IMF	International Monetary Fund
IPE	International Political Economy
IR	International Relations
MacPR	Macro-prudential regulation
MCMD	Monetary and Capital Markets Department
MicPR	Micro-prudential regulation
NDB	New Development Bank
UMPs	Unconventional Monetary Policies
VAR	Value at Risk
WEO	World Economic Outlook
ZLB	Zero Lower Bound

Abstract

In 2008 the neoliberal economic ideas steering the course of global economic governance seemingly collapsed as the world entered into the greatest financial and economic crash since the Great Depression. Initially a range of precipitating causes were offered including lax monetary policy and a miss-pricing of risk, common to which was an assumption that although severe, the downturn was limited to policy failures in a relatively stable economic framework, and therefore constituted a crisis *for* neoliberal global economic governance.

As the downturn intensified however, there developed a consensus that the situation facing policymakers was not simply a crisis for neoliberal global economic governance, but more fundamentally a crisis *of* neoliberalism which was now interpreted as a major precipitating cause. Therefore just as the failure of Keynesianism presaged a shift to neoliberalism, so too was there an expectation that its failure would exert a similarly transformative dynamic.

Against this backdrop this research investigates the extent to which the neoliberal economic ideas steering the course of global economic governance are characterised by change or continuity. This is explored through the examination of an institution commonly assumed a bastion of neoliberalism, the IMF, and with specific reference to two areas synonymous with neoliberal economic ideas, monetary and fiscal policy, and financial sector liberalization.

The research points to two reasons to suggest the potential for change. Firstly, many of the neoliberal economic ideas advocated by the IMF were cognitively falsified by the severity of the economic downturn. Secondly, as the downturn unravelled, the IMF advocated a range of policy interventions that had been considered largely anathema only months previously.

Nevertheless, the key finding of this research is that to suggest this was the beginnings of a major shift was to miss-read the intentions of those tasked with responding to the crisis who were more concerned with preserving, as opposed to altering, the status quo. As a result, it is demonstrated that the IMF remains committed to the neoliberal economic philosophy (assumptions made regarding the efficacy of the market as opposed to state intervention) which has vital implications for the way in which economic problems continue to be interpreted and responded to, and the kinds of policies considered appropriate.

Introduction

In 2008 the neoliberal economic ideas steering the course of global economic governance – a set of assumptions regarding the appropriate means by which to organise economic activity – appeared to collapse as the world witnessed what has been broadly contextualised as the worst financial and economic downturn since the Great Depression (Hay, 2011:2). Beginning initially in the sub-prime mortgage market of the US financial sector, the downturn quickly precipitated a broader credit crunch which spilled over into the real economy, negatively affecting economic growth and employment the world over.

Initially, the collapse was variously conceptualised as the result of lax monetary policy (Carmassi et al, 2009), a values crisis (Friedman and Friedman, 2008), or a mispricing of risk worldwide (Greenspan, 2008). Although clearly saying something different, common to these diagnoses was an assumption that, although serious, the downturn was the result of flawed policies deployed in an otherwise effectively functioning overall framework. As time progressed however, there developed something of a consensus that its implications were far more fundamental; that is, a major failure of neoliberal economic ideas and policies.

This rendered as fallacy the assertion that neoliberalism provided the sole, inevitable, most efficacious, one best way by which to steer the global economy, and instead, drew our attention to actual existence of the potential for a range of political-economic alternatives, with each characterised 'by divergent interpretations of the opportunities or constraints presented, a view of what should and should not be subject to discussion or regulation, and ideas as to how best to strategically organize the direction of collective action' (Cerny, 2008:5).

Certainly, with the downturn increasingly recognised as one of the three great crises of capitalism along with the Great Depression of the 1930s and Great Inflation of the 1970s, (Gamble, 2009:452), both of which precipitated substantive change, it was not uncommon to assume that the present downturn would exert a similarly transformative dynamic in the economic ideas steering the course of global economic governance. Indeed, Blyth (2012:10) suggested that 'if there was ever a perfect case for a "paradigm shift"... surely this was it'.

In light of this discussion this research addresses two key questions.

- Given their evident failings, to what extent are neoliberal economic ideas characterised by change or continuity?

In answering this question, this research draws on the IMF as a case study to demonstrate how - although the failure of neoliberal economic ideas provided the pre-conditions from which to enact a major transformation in the economic ideas steering the political economy, the ways in which economic problems continue to be interpreted and responded to, and therefore the kinds of policies considered necessary - change has not been forthcoming.

This claim is substantiated through reference to two policy areas synonymous with neoliberal economic ideas in the IMF. Firstly, the research draws on the example of economic policy to demonstrate how during the most acute phase of the downturn the IMF broke with orthodoxy by calling for substantial fiscal stimulus in order to shore up aggregate economic demand, a move considered at the time as having the potential to exert a transformative dynamic in economic policymaking in the IMF.

This potential notwithstanding, this research suggests that such a shift never materialised as calls for fiscal stimulus, from their earliest inception, were couched in orthodox assumptions of the need for fiscal sustainability. Therefore as the most acute phase of the downturn passed, the IMF called for major fiscal adjustment through the enactment of a range of policies consistent with as opposed to those provided by neoliberal frames of reference.

Secondly, the research draws on the example of financial sector liberalization and deregulation, and in doing so, demonstrates how the hands-off regulatory approach was interpreted by senior officials within the IMF as a major precipitating cause of the downturn (Strauss-Khan, 2008c). As a result, space seemingly opened up for more significant government intervention into the functioning of financial markets through the enactment of a range of policies considered off-the-table only months prior. This raised expectation of the potential for a major transformation in the manner in which the efficacy of government interventions into banking and financial sectors were once again understood.

Nevertheless, just as was the case with economic policy, this research suggests that such a shift never materialised. Rather, banking and financial sector reforms continued to be couched within the broader context of continuing adherence to belief in the efficacy of neoliberal economic ideas. As a result, there was no major change in the manner in which economic problems were interpreted and responded to as the IMF, once the most acute phase of the downturn had passed, called for caution in the regulatory debate.

- Why did the monumental failure of neoliberal economic ideas not lead to a broader crisis of the neoliberal order?

The starting point here, in light of the preceding discussion, is that the failure of neoliberal economic ideas did not lead to a crisis in the constructivist sense in which the moment of failure is inter-subjectively interpreted by actors as requiring altered structures (change). Indeed, for it to be seen as such would require that adherence to neoliberal economic ideas be interpreted as a precipitating cause of the downturn, yet this is currently not the case.

That constructivist approaches are typically deployed to account for the processes by which crises bring about significant transformations might appear to suggest that they lack an adequate conceptual framework with which to account for questions related to continuity. As a result, rational choice approaches with their emphasis on stability and continuity might appear, superficially, well positioned to provide us with a suitable explanatory account.

Nevertheless, a key assumption of this research is that a constructivist approach provides us with a more interesting and fruitful avenue of enquiry by which to understand the mechanisms deployed by the IMF to construct continuity in economic ideas. In the process of outlining the case for such an approach, this research takes up the challenge by Schmidt (2011:111) 'to find less deterministic and more dynamic ways of thinking about continuity'.

By way of substantiating this claim it is suggested that, just as actors seek to effect change through crisis construction and the provision of narratives of what went wrong, so too are those seeking to defend and maintain the status quo engaged in this ‘war of competing narratives’ (Hay, 1999:336). Indeed, that actors ‘typically confront resistance from defenders of the status quo’ (Chwieroth, 2010:501) means there is nothing to suggest that those motivated by change will be successful in their endeavours to shape responses.

This acknowledgement is certainly not controversial. However, what is missing from much of the constructivist literature is an analysis of the means by which actors engage in such a process. For the purposes of this research, two are explored, both of which are inherently constructivist. On the one hand, the historical analogy literature associated with

International Relations (IR) is drawn upon to demonstrate how the IMF sought, during the initial stages of the downturn, to reduce unravelling uncertainty. It did so by interpreting events through existing knowledge structures (neoliberal economic ideas) which provided a mechanism by which to compare the unfolding turmoil with similar instances from the past to both help deal with indeterminacy in the present, and crucially, to derive policy lessons.

On the other hand, the sociology literature is drawn upon to highlight the importance of framing which is shown to have been deployed as a means to assign meaning to unfolding events. In doing so, it is demonstrated how the IMF played a crucial diagnostic role in drawing attention to the importance of particular problems, along with a prognostic role in advancing policy solutions to the problems so-defined.

Case study justification

This research draws on the IMF as a case study. The rationale for doing so is three-fold. Firstly, the IMF was tasked by the G20 group of state leaders with playing an important part in diagnosing and responding to the global economic downturn. Moreover, at the G20 leader's summit at London in early 2009, the resources made available to the IMF were increased significantly so that it would be suitably positioned to respond to requests of assistance by countries struggling to cope with the worst effects of the downturn. Together therefore, we can see how the IMF was accorded a pivotal role in developing responses.

Secondly, the IMF is located in a broader architecture of global economic governance which seeks to coordinate broad agreement on policy priorities. Moreover, it plays a critical role in providing cognitive justification, and thereafter communicating, the economic ideas developed in the coordinative discourse through the dissemination of research which seeks to persuade other actors of the efficacy of problem definitions and policy positions. In doing so the IMF constitutes 'an important conduit of influence for economic ideas' (Clift, 2013:1).

Thirdly, that the IMF has often been referred to as a bastion of neoliberalism makes it a particularly fruitful case study (Peet, 2009). Nevertheless, neoliberal economic ideas cover a large range of areas. As a result, in order to illuminate this research, focus is placed on two policy case studies, monetary and fiscal policy; and financial sector liberalization and deregulation, each of which have become synonymous with neoliberal/IMF policy discourse, and were characterised by varying degrees of failure during the current downturn.

In the case of the former, policy-makers seeking to influence economic output have two main tools at their disposal – monetary policy, in which central banks indirectly target activity by influencing the money supply through, for example, adjustments to interest rates and bank reserve requirements; and fiscal policy, in which governments influence economic activity by changing the level and types of taxes, and the extent of spending.

The relative weighting allocated to each approach has typically waxed and waned. Post World War 2, fiscal policy was considered *the* macro-economic policy tool in the IMF. Nevertheless, by the 1980s, monetary policy had assumed prominence as the primary means by which to manage the economy (particularly during downturns/recessions) and therefore became a key focus of policy advice to countries borrowing from the IMF.

The oscillation from fiscal to monetary policy was premised in large part on new research. This was summarised by former First Deputy Managing Director of the IMF Stanley Fischer (1993:2) who noted that fiscal policy: arrived too late due to implementation lags; was distorted by political constraints; reduced private investment by raising interest rates; and was largely redundant as monetary policy was capable of maintaining a stable output gap.

Although it would be unwise to confuse correlation with causation, an assumption was made within the IMF that the privileging of monetary policy in managing the economy (manipulating the policy rate to counter recessions) and a solid anchoring of inflationary expectations had helped to reduce the effects of shocks on the economy. Economic ideas therefore, ostensibly supported by empirical evidence, led Blanchard et al (2010) and Vinals (2009) to note that better policymaking had delivered higher economic growth and stability.

This notwithstanding, as the downturn unfolded, fiscal policy again assumed prominence in IMF policy advice. Indeed, from advocating monetary policy interventions during the initial phase of the downturn, the IMF rejected orthodoxy and, for the first time in its history, called for globally coordinated fiscal stimulus in order to shore up ailing demand, and in doing so seemingly reverted to an apparently discredited set of Keynesian economic ideas.

This move, along with the fact that economic policy has been shown to be characterised by shifts in 'conventional wisdom' following major events such as wars and major financial crises (Cukierman, 2013:1), meant the current downturn appeared to offer an opportunity with which to affect a similarly transformative dynamic. Together therefore, we can see how economic policy provides this research with a particularly fertile ground for study.

In the case of the latter, although controls over financial activity were initially advocated by the IMF, financial sector liberalization and deregulation came to develop an inextricable synonymy with IMF policy discourse. Then Managing Director of the IMF Michel Camdessus (1997:1) summarised the benefits, including that they: give countries new opportunities to quicken the pace of investment, job creation, and growth; give investors a wider range of investments along with higher returns on savings; and promote a more efficient allocation of resources worldwide, thereby contributing towards stronger world growth.

These apparent benefits notwithstanding, financial liberalization and deregulation has been accompanied by an increasing number of financial and economic crises. In response, and in recognition that crises were an increasingly inescapable part of the contemporary global financial landscape, global economic governance institutions advocated the creation of two Basel accords (Basel 1, 1988; and Basel 2, 2004) which encouraged banks to hold a greater degree of capital so that they would be suitably positioned to meet their financial obligations in the event of a downturn. These were supported by the IMF which provided technical assistance to member states in the implementation stage.

The two Basel accords were underpinned by a micro-prudential approach to regulation (MicPR) which was grounded in an assumption that minimising the risk of failure by individual institutions through deposit insurance and other safety nets, along with special insolvency and resolution mechanisms, would make the financial system as a whole more resilient. Moreover, it was thought that regulating banks (no matter how minimally) would ensure that lending outside the core would capture systemic risks, and that, applying regulation to non-banks (and financial instruments) would be costly, reduce innovation, and actually increase systemic vulnerabilities by inhibiting the ability of markets to transfer risk.

It was therefore assumed that banks should be allowed to engage in almost any form of financial activity so long as it had robust risk management systems and sufficient earnings to support underlying risks. In short, such an approach would, it was suggested, liberalise the powers of well-managed banks to spur innovation and economic growth (Zamil, 2009:1).

This notwithstanding, that the origins of the downturn were in the banking and financial sectors at the very heart of global financial capitalism (the US) before spreading globally led many (Brown, 2009; Stiglitz, 2009) including senior IMF officials (Strauss-Kahn, 2008c), to deduce that the hands-off approach of the preceding years was fundamentally flawed.

Therefore, just as the renewed emphasis on fiscal interventions constituted a potentially fundamental shift in economic ideas in the IMF, so too was a similar assumption made of the need for a fundamental overhaul in the regulation of the banking and financial sectors in order to prevent a recurrence. Although a number of areas of reform were highlighted, including the need for greater liquidity ratios and regulation of globally significant banks, this is explored through the most developed area, Basel 3, which seemingly created space for much greater government intervention into the functioning of financial markets.

Methodological approach

Although it has been suggested that there is no intellectual reason why a rational choice approach be particularly amenable to a quantitative methodology, nor that a constructivist approach should be especially well suited to a qualitative methodology, (or that they are mutually exclusive), Farrell and Finnemore (2008:60) have nevertheless demonstrated that near-zero constructivist IR/IPE research employs quantitative techniques. This suggests an especially strong correlation between a constructivist approach and a qualitative methodology.

This research proceeds in a broadly similar vein in acknowledging that although 'both qualitative and quantitative methods may be used appropriately with any research paradigm' (Guba & Lincoln, 1994:105) generally speaking a quantitative methodology is particularly useful in conjunction with orthodox theory whereas a qualitative methodology is especially amenable to the constructivist approach taken to this research.

With this in mind, the research questions posed above are addressed through a qualitative methodological approach. This is however, 'a broad umbrella term that covers a wide range of techniques and philosophies' (Hennink et al, 2011:8) including in-depth interviews, focus group discussions, observation, visual methods, life histories and biographies among others, but is nevertheless limited for this research to a text analysis of official IMF documents.

This approach taken to this research is therefore interpretive, relying on less formal methodologies which are de-emphasised to make room for a wide range of analytical concerns, each typified by differing methodological approaches (Cohen, 2007:200). In particular however, this research draws on insights provided by post-modernist/post-structuralist approaches and hermeneutics.

Firstly, post-structuralism and post-modernism have contributed to the understanding that there is no clear window through which to observe an objective reality as any gaze is always filtered through, for example, the lenses of language and social class (Denzin & Lincoln, 2000:19). As a result, such approaches are critical of attempts to ground knowledge in objective and essential foundations. Rather, an assumption is made that to make sense of an action we have to interpret it in the wider prior discourse of which it is a part, as actions are only understandable in an episteme or framework of meaning which helps to construct individuals and their beliefs.

This approach is therefore concerned with the analysis of ideas and discourses and how these perform within and frame practices and institutions. It is important in drawing our attention to the fact that conceptions and interpretations of reality presented in texts are socially constructed within the wider context characterised by social, historical and cultural particularities within which, for our purposes here, the IMF operates (Hennink et al, 2011:15).

The broader context is therefore critical precisely because it provides us with 'a set of ideas, concepts and rules about how one thinks and talks about a topic' (Yates, 2003:233) as well as the knowledge a group (for our purposes here, global economic institutions) have about a particular topic (the appropriate means by which to steer the international political economy).

Moreover, these ideas and system of knowledge include the construction of specific interpretations and understandings of concepts which together are a product of, contain language forms and practices defined by, and help to recreate and support that very system. Viewed in such a manner, knowledge does not reflect a purported social reality, but produces meaning, creates social reality, with different discourses and languages dividing up that world in order to give it meaning (Richardson, 2000:928-929).

For our purposes here, we can therefore see how these systems of knowledge provide IMF staff with an interpretive lens which provides a perspective that makes assumptions regarding how the international political economy should be understood and studied. In doing so particular demands are made on staff (implicit or otherwise), including the kinds of questions they seek to answer, thereby simultaneously guiding and constraining work that will be conducted (Denzin & Lincoln, 2000:18-19).

This approach suggests that subjects experience the world in ways which depend on the influence of social structures on them. However, this is accompanied with the caveat here that they are also endowed with sufficient agency to alter these structures by adapting, developing, or rejecting existing ideas and institutions. Moreover, also engaged in attempts to shape the broader context are those motivated by seeking to entrench the status quo by engaging in persuasive struggles that draw on existing interpretations, understandings and conceptions. Together therefore, we observe here a discursive sphere in which actors compete to shape shared meanings which act as the subsequent background for action.

The approach taken here therefore allows us to overcome a problem often directed at methodological approaches which study text, that is, they are typically assumed to interpret texts without contexts. In doing so, it is demonstrated how the commitment of global economic governance institutions (including the G7/20 and IMF), to a particular set of neoliberal economic ideas addresses this criticism by noting that it is not just ideas or text that is important (what is said), but also context (by who, when, and where) and purpose (what is the aim of such research in terms of the policies advocated) (Schmidt, 2008:305).

Secondly, further to the preceding discussion, this research incorporates insights derived from hermeneutics which takes as its point of departure the inherent subjectivity of perceptions of reality. Doing so suggests the potential for a range of perspectives, with each characterised by a multiplicity of meanings and competing interpretations (Hodder, 2000:879; Yanow & Schwartz-Shea, 2006:390). Viewed in such a manner, the producer of a text 'is merely an interpreter whose own account has no greater claim to 'truth' than anyone else's account. There can never be a final accurate representation' (Devine, 2002:203) of reality, simply differing interpretations.

An assumption is therefore made that the production of knowledge is shaped by the researchers' perspective. This serves to demonstrate that what is often presented by the IMF as common sense is in fact incomplete and only held provisionally as we do not perceive the world without pre-established conceptual boxes and traditions which structure perspectives, as the preceding discussion demonstrated (Bevir & Rhodes, 2002:135).

That is, researchers' positionality, the cognitive-emotional dimensions, the impacts of interests on judgements means that research is inherently complex as meaning does not exist independently of our understanding of it, but is reflective of our interpretation of it.

The approach deployed here therefore rejects positivist assumptions of knowability and the analogy that such scholars postulate between the natural/physical worlds, and the social world, which is shown to be false. That is, unlike rocks and atoms, humans communicate, share, interpret and contest meaning such that our institutions, ideas, policies and language are shown to be human creations that do not exist independently of us (Yanow, 2006:7).

In doing so, an assumption is made that research is not, nor can ever truly be, value-free in which researchers have no influence on data collection or interpretation. If we accept this premise, then it becomes clear that research is in fact undertaken, and guided by, a set of beliefs and feelings about how the world is, how it should be understood, and most pertinently for this research, how it should be studied (Denzin & Lincoln, 2013: 19-23).

As a result, research produced by the IMF contains but one particular array of signifying elements that set the parameters of a cognitive window through which a text is seen. That is, the intended meaning of research is to direct attention as well as restrict the perspectives available to its intended audiences. Viewed in such a manner, texts are understood here as structurally located choices of concepts following certain shared rules and conventions. In essence, they are tools used in composing and constructing a particular discourse.

By drawing on the hermeneutic approach this research therefore highlights the social, cultural, and most particular for our purposes here, institutional dynamics associated with the production of texts. Indeed, accepting the absence of an objectively identifiable 'real world' means that it is not possible for IMF research to claim a privileged position that enables it to engage in the production of authoritative knowledge. Rather, the approach taken here draws attention to textual claims to authority, that is, the incomplete knowledge claims made by the IMF.

This approach is inductive, thereby allowing for the capture of inter-subjective meanings, is historical in that it aims to develop an historical narrative, deconstruct and de-naturalise the economic ideas and knowledge constructs which the IMF uses to legitimate its actions, and allows for an exploration of the manner in which texts contribute to understanding reality. Moreover, it creates space for alternative ideas and understandings, and by implication, the potential for change as well as continuity (see for example Kincheloe & McLaren, 2000:286).

Data selection

The preceding discussion provides us with an interpretive methodological approach which draws our attention to the fact that to better understand the intent, background and history of those engaged in the production of research, it is necessary to locate it within the broader context in which it is produced (Yanow, 2006:15). As a result, given that knowledge is not simply 'out there' as some inert form of nature, it is necessary to study texts, or more specifically for our purposes here, research output and speeches derived from the IMF, as texts do not just represent themselves, but are socially constituted and constructed.

This nevertheless begs the question as to how an interpretive approach might apply to and help us to understand the kinds of claims that the IMF makes, namely, which texts produced by the IMF are most likely to provide satisfactory answers to our research questions.

Here the research borrows from Weldes (2006:178) the distinction between "high" and "low" data. Although there are obvious synergies between the two, the former is the focus of this research as it is that which circulates among elite institutions of the coordinative discourse, whereas the latter is more commonly associated with popular and mass culture.

Superficially at least, this may appear an onerous task given the IMFs considerable research output. This includes for example: the IMF's bi-annual flagship publication the World Economic Outlook (WEO); five Regional Economic Outlooks (REOs) produced by the various area departments; Special Issue Papers (SIPs) that accompany Article IV consultation documents produced by area departments; Occasional Papers (OPs) that feature nontechnical analyses of economic and financial subjects of current importance to the IMF; and Policy Discussion Papers (PDPs) and Staff Discussion Notes (SDNs) that showcase new policy analysis and research by IMF departments. Indeed, in all, the IMF produces over five hundred pieces of original research per year, equivalent to between four and five thousand for the period covered by this research (IEO, 2011:7).

Nevertheless, the policy case studies selected for the purposes of this research narrow the issues for analysis, and by implication, the number of texts that can be considered suitable for selection. As a result, analysis is focused primarily on the bi-annual publications the Global Financial Stability Report (GFSR) and Fiscal Monitor, Working Papers and Policy Papers, and playing a supplementary role, speeches made by senior IMF officials.

Firstly, the analysis of fiscal policy draws upon research presented in the Fiscal Monitor (FM) which was established in 2009 by the Fiscal Affairs Department (FAD) of the IMF. It arose specifically in response to the fiscal effects of the economic downturn (the use of fiscal stimulus and its negative implications for sovereign debt burdens) as a means by which to both track fiscal responses by member states, and crucially for the purposes of this research, seek to influence the direction of action by providing policy relevant analysis.

Secondly, the analysis of financial sector liberalization and deregulation draws on the Global Financial Stability Report (GFSR), created in 2002, and produced by the Monetary and Capital Markets Department (MCMD) of the IMF, its aim being to be a centre of excellence for all aspects of financial, capital market, and monetary work. In doing so, the GFSR, in tracking emerging risks and highlighting what the IMF perceives as being the most salient vulnerabilities and threats to global financial stability, forms the main surveillance vehicle of the IMF. Moreover, and of particular importance for this research, the GFSR, particularly through its analytic chapters which address topics relevant to current policy discussion, plays a critical part in drawing attention to the IMFs evolving views on lessons from the downturn, as well as providing policy relevant analysis (Kiguel, 2011:1).

Thirdly, this research draws on Working Papers and Policy Papers produced by FAD and MCMD Departmental Directors and staff members, along with other senior officials including Managing Directors, Deputy Managing Directors and Research Director. Focusing on research conducted by such officials allows us to stay as true as possible to the official stance taken by the IMF. Moreover, in doing so this research overcomes a problem highlighted by the IEO (2011:3) that a number of Working Papers produced by junior staff members have the potential to be released without official authorisation, and as a result, they can, in theory at least, produce analysis that is inconsistent with official IMF responses.

Finally, speeches by senior officials within the IMF are an especially useful supplementary source of enquiry as, like research, 'they are precisely intended to sell a particular representation' (Weldes, 2006:181) of established problem definitions and policy priorities. Therefore, speeches do more than simply say things, they have both a practical and social function inasmuch as they are similarly rife with, and help to communicate, the dominant discourse to as wide an audience as possible in order to help ensure its propagation.

By exploring these texts, this research draws on two types of economic research ("high" data) carried out by the IMF, each of which is critical in helping to determine the extent to which it is possible to adjudicate between change and continuity in economic ideas.

Firstly, the GFSR and Fiscal Monitor are surveillance and policy oriented. As a result, they allow for the potential to determine at one level the extent to which policy priorities changed during the economic downturn when considered against those advocated prior. This approach has been characteristic of much of the academic literature that has sought to adjudicate the extent to which the IMF is characterised by change or continuity (see Babb, 2009; Ban & Gallagher, 2014; Grabel, 2011; Guven, 2012 Wilson & Grant, 2013).

Secondly, Policy Papers, and in particular Working Papers, are academic in style inasmuch as they feature original research by IMF staff and therefore seek to generate new knowledge to deepen understandings of policy frameworks. That is, they are empirical, descriptive, theoretical and more technical than other research products (IEO, 2011:1-4). In this regard, analysis of their content throughout this research affords us the opportunity to go beyond an investigation of the policy realm, to providing a much deeper exploration of the extent to which the underlying economic philosophy (assumptions made regarding the efficacy of free markets in the functioning of the political economy), and manner in which economic problems are interpreted and responded to, are characterised by change or continuity.

Taken together therefore, textual evidence derived from this research enables us to explore the central representations offered by elites (Weldes, 2006:181). This allows for the generation of a portrait that illuminates a well rehearsed set of narratives that provide justification for particular policy priorities, and which are intimately linked to problem definitions and the broader underlying economic philosophy. Indeed, it is this research that helps to create, advocate, communicate and hold together the prevailing discourse.

The preceding discussion however does lead us to an important question. To what extent can we take this research, along with speeches by prominent officials, as a reasonable proxy for IMF thinking so that we are suitably placed to adjudicate between continuity and change? In answering this question it is suggested that we can for two important reasons.

Firstly, it is suggested here that the broad research agenda in the IMF is shaped by a number of key actors within and beyond the IMF. On the one hand, outside of the IMF the G7 plays a crucial role in steering the broad direction, and thereby setting the general agenda, of global economic governance institutions by emphasising broad principles. Moreover, it exercises the power of instigation for more technical institutions, including the IMF, for which it relies on, and has the power to endorse, more specialist knowledge present in its research output.

On the other hand, the Executive Directors within the IMF can shape agendas and endorse research which is presented and discussed by the Board (IEO, 2011:19). This is crucial as, having access to all of the IMFs research output, the Board act as active consumers, particularly of the analytical chapters of the WEO and GFSR which are routinely presented to and discussed by its members. In a similar fashion, the Managing Director and Deputy Managing Directors assume an important role in planning and coordinating research.

Finally, research conducted by the IEO (2011b) has shown that in the functional departments with which this research is concerned, top-down direction is common. The FAD for example was shown to be increasing its control from the centre over time, maintaining a list of important research topics, while issues were discussed with senior staff and priorities were set in collaboration with senior management. In a similar fashion, research undertaken by the MCMD was consistent with a prioritised agenda at the time senior members of staff were interviewed. Together, this suggests a particularly important role for the most senior officials in shaping the general direction of its research output.

Second, given the foregoing discussion, an assumption underpinning this research is that there is very little, if any, scope for IMF staff to exercise a considerable degree of intellectual innovation and thereby contribute to the broader economic debate in a manner that is inconsistent with senior officials. Rather, it has been suggested that IMF staff exhibit a strong tendency to tailor research plans and conclusions to fit with the existing economic philosophy, problem definitions and policy positions (see for example BWP, 2011a:1).

Research conducted by the IEO (2011:10) supported this assumption by showing how almost two thirds of IMF staff in response to an IEO questionnaire, stated that research and conclusions had to be aligned in a manner consistent with official IMF views. The corollary of this however is that the potential for alternative, more heterodox approaches are essentially evacuated at the earliest stage of policy discussions. In doing so, this helps us to understand the considerable degree of consistency among IMF research output.

The research findings provided by the IEO were further compounded with personal e-mail correspondence undertaken during the course of this research with officials from the Fiscal Affairs and Monetary and Capital Markets Departments. When questioned of the extent to which individuals considered whether or not economic ideas in the IMF were characterised by change or continuity, respondents at no point deviated from the official line provided by the IMF. Rather, they consistently stated that the most appropriate means by which to understand its position was to be found in official publications including Working Papers and Policy Papers produced by senior IMF officials.

Taken together therefore, this suggests that there was little or no scope for intellectual innovation, and thereby space, in which to push for more fundamental challenges, and more significantly, changes, to extant economic orthodoxy as a result of the downturn. Rather, research produced by IMF staff continued to exhibit a considerable degree of consistency in the manner in which economic problems were understood and the kinds of policies considered desirable, which are themselves a reflection of the broader underlying economic philosophy. As a result, we are suitably placed to state with some degree of conviction that such research can indeed be taken as a viable proxy for IMF thinking.

Outline of the research

With the preceding discussion in mind, this research proceeds as follows. **Chapter 1** sketches out the efficacy of a constructivist IR/IPE approach as the most efficacious means by which to explore the research questions posed above. Doing so allows for the development of an approach which both accords a causal role to ideas; and provides a dynamic view of change (or continuity) in the context of crisis.

In the first of the context chapters **Chapter 2** situates the IMF in historical context by offering a brief historiography of its creation and initial remit, with emphasis on the Keynesian economic ideas underpinning its creation and the system of fixed but adjustable exchange rates. Thereafter it is demonstrated how the end of the Bretton Woods System in 1973 along with rising inflation and declining growth rates precipitated a shift in the raison d'etre of the IMF and the economic ideas underpinning policy actions which were increasingly informed by the neoliberal economic philosophy and problem definitions.

This notwithstanding, it is demonstrated how beginning with the developing country debt crisis of the early 1980s, the IMF was drawn back into crisis management and lending. In doing so, policy advice was increasingly underpinned by neoliberal economic ideas which were deployed in order to stabilize affected economies through monetary/fiscal discipline, and provide longer-term structural adjustment policies aimed at correcting underlying economic problems. Key in this process was the assumption that countries approaching the IMF had pursued un-sustainable policies and would require a greater degree of intervention than was the case in balance-of-payments crises that had characterised the post-war period.

The second of the context chapters, **Chapter 3** serves two purposes. Firstly, a background to the financial and economic downturn is provided. In doing so, it is suggested that, although initially conceptualised as the result of policy failures in an otherwise effectively functioning economic framework, the downturn can be best interpreted as the result of two policy failures inherent to neoliberalism, economic policy, and financial sector liberalization.

Secondly, the chapter outlines the manner in which events were interpreted and responded to by the IMF and in doing so, suggests that responses be best understood as having progressed through a series of related yet distinct phases. The first of these was limited to failings in the banking and financial sectors; the second phase occurred as events spilled over into the real economy, negatively affecting economic growth and employment; and the third phase occurred as fiscal interventions during the second phase substantially increased sovereign debt, thereby raising solvency concerns. Understanding the downturn like this is crucial to this research as each phase: required a diverse set of policy interventions; had important implications for the manner in which economic problems were interpreted and responded to; and had differing implications for the economic philosophy in the IMF.

In the first of the case studies, **Chapter 4** turns the attention of the research to fiscal and monetary policy. In doing so, it is demonstrates how, during its first phase the banking and financial sectors were characterised by declining bank liquidity amid rising uncertainty which ultimately precipitated a slow-down in economic activity. In response the IMF, in a manner consistent with neoliberal orthodoxy, advocated the deployment of conventional monetary interventions (reducing the policy rate), and latterly, unconventional monetary policies (UMPs) (forward guidance of the policy rate) as the first line of defence.

Given their inability to stem the turmoil, and prevent the transmission of the banking and financial deficiencies to the real economy however (the second phase), the chapter charts how the IMF broke with orthodoxy and 'for the first time in its history, called for a global fiscal expansion across all countries' (Cottarelli, 2013:1), a move interpreted at the time as a potentially epoch-shaping shift in economic philosophy in the IMF (Clift, 2013).

Chapter 5 however suggests that the failure of monetary policy interventions (conventional or otherwise) and subsequent call for fiscal stimulus notwithstanding, as attention turned towards sovereign debt sustainability (the third phase) it became increasingly evident that the IMF continued to retain a normative commitment to the prevailing economic philosophy and the manner in which economic problems are interpreted and responded to.

As a result, despite the failure of existing economic ideas there was no wider crisis resulting in changed structures underpinned by new economic ideas. Indeed, the IMF, if anything, is shown to have attempted to frame the third phase (sovereign debt concerns) in such a manner that the further entrenching, not retreat from, policies consistent with neoliberal economic ideas were necessary to reduce excessive sovereign debt burdens.

In the second of the case studies, **Chapter 6** highlights how, as the banking and financial sector deficiencies began to unravel during the first phase of the downturn, it was apparent that allowing banks to increase leverage and lower capital buffers while increasing their exposure to risk was severely misguided and that it would be necessary to move towards a financial system characterised by less leverage and greater capital ratios. Initially however, the IMF framed the unfolding turmoil as being the result of supervisory, not regulatory, failures which were resolvable within existing frames of reference, a commitment couched in the need to better supervise the implementation the Basel 2 capital accords.

This notwithstanding, as the downturn spilled over to the real economy (the second phase), it was apparent that simply supervising the implementation of the existing Basel accords would be insufficient, and that more substantive regulation would be required in order to prevent a recurrence. As a result, the IMF advocated the creation of a new set of rules (Basel 3) which would double capital requirements and introduce additional conservation and counter-cyclical buffers to counter the system-wide vulnerabilities of banks. This suggested a much greater role for the state in the regulation of the banking sector and with it, the potential for a shift in the prevailing economic philosophy in the IMF.

This ostensible shift notwithstanding, **Chapter 7** suggests that as focus turned towards sovereign debt sustainability concerns (the third phase) two developments suggested that the regulatory landscape was, in fact, equally, if not more liable to be characterised by continuity as it was change. Firstly, as the global economy improved, risks to financial stability subsided, bank capital needs declined or were declining substantially, and attention turned towards the rapid accumulation of public debt, thereby contributing to a re-focusing of the reform agenda (GFSR, 2010:2). Secondly, as 2011 progressed, a subtle but noticeable shift in IMF research output emerged which, concerned with addressing the cost implications of additional regulations, called for caution in the capital adequacy debate.

Although there therefore appeared to be a clear direction within the IMF for reform during the second phase, implementation was becoming increasingly spoken of as something for the future. Against this backdrop, Kodres and Narain (2010:4) of the MCMD suggested two potential regulatory scenarios: (1) having skirted economic collapse, the official community allows complacency to set in, allowing reforms to languish; and (2) the severe effects of the downturn lead public bodies to respond vigorously, contributing to over-regulation to such an extent that certain markets simply disappear. The chapter demonstrates how it is the former of these scenarios that played out.

Finally, by way of conclusion it is noted that the downturn has induced some policy change in the IMF. On the one hand, the recognition that counter-cyclical fiscal policy is more efficacious than was thought prior seemingly implies the potential for a more substantial role for government intervention during times of severe economic dislocation. Similarly, of banking and financial regulation, the shift to Basel 3 seemingly represented an important step in recognising the inadequacy of the previous framework and implied the potential scope for greater government intervention into the functioning of financial institutions.

Notwithstanding this ostensible shift, an assumption is made that on a more fundamental level the IMF continues to retain a normative commitment to the prevailing economic philosophy and the manner in which economic problems are interpreted and responded to.

On the one hand, although the IMF acknowledged the efficacy of fiscal policy interventions, this was only recommended in exceptional circumstances such as those analogous to the current downturn. As a result, there was no suggestion that counter-cyclical fiscal policy might become a more significant part of the future policy mix. Rather, the IMF has consistently made clear that monetary policy retains primacy for the functioning of the economy and management of less severe downturns.

Likewise, on the other hand, the new Basel accords remain very much entrenched within prior intellectual frames of reference, albeit with some minor modifications. Indeed, of the financial sector, the IMF very much remains an institution committed to financial sector liberalization and deregulation and thereby only a minimal scope for state intervention.

Chapter 1
Theoretical approach

'Everything conspires to make us forget the socially constructed'
(Pierre Bourdieu)

Introduction

This research is an enquiry into the nature of continuity in economic ideas, along with an exploration into the manner in which this has been constructed by the IMF. In this respect, a constructivist IR/IPE approach, with its emphasis on the dynamic roles played by ideas, identities, interests, and assumptions made regarding the inter-subjective bases of everyday reality as key in shaping political economic process and outcomes is well suited to this end.

These basic insights and their relevance to this research is fleshed out hereon in by drawing on Schmidt's (2008, 2010) distinction between an institution's *coordinative discourse* (the role played by apex policy forums in developing the economic philosophies and problem definitions steering global economic governance); and *communicative discourse* (the means by which the IMF provides justification for their associated policy priorities which are subsequently disseminated through research output and speeches by senior officials).

Thereafter, outlining a constructivist approach to crisis and change serves as a pre-cursor to developing an argument that suggests that a constructivist conceptual vocabulary centred upon the politics of framing, narratives, the interpretation of events, and the role of persuasion leaves us ideally placed to understand continuity in economic ideas in the IMF.

In particular however, two methods deployed by the IMF to construct continuity are explored, both of which are inherently constructivist. Firstly, drawing on the concept of historical analogy associated with IR literature, it is demonstrated how actor's reason through historical analogy to reduce uncertainty associated with seemingly novel problems to make the political-economic environment more knowable, and to derive policy lessons.

Secondly, drawing on the sociology literature associated with framing, it is demonstrated how actors seek to assign meaning to unfolding events. Notably, framing is shown as having two key functions, firstly, as a diagnostic tool in assigning meaning to events, and secondly, as a prognostic tool in advocating particular policies to deal with the problem so defined.

Constructivist approach to global governance analysis

Not in and of its self a theory in the sense of subjecting hypotheses to empirical testing, constructivism can be best understood as an *approach* to IPE characterised by certain ontological assumptions, chief among which is a conception of social science that is, social (Kratochwil, 2001:15). While accepting the presence of a material world, constructivism draws our attention to the fact that many purported material facts of the international political economy are actually 'shaped by human action and interaction which depends on normative and epistemic interpretations of the material world' (Adler, 1997:322).

By drawing our attention to the fact that the building blocks of the international political-economy 'are ideational *as well as material'* (Ruggie, 1998:33, emphasis added), a constructivist approach eschews both the notion of contextually predetermined ideas and interests at one end of the theoretical spectrum, along with the contrasting assumption that 'only ideas matter and can be studied' (Adler, 1997:321). Rather, actors are understood as not being solely motivated by a set of material and/or objective interests, but instead act on a range of reasons such that one cannot distinguish objective interests from ideas. What is important for constructivists is developing a greater understanding of the manner in which interests come to be perceived as such and subsequently acted upon (Schmidt, 2008:317).

The commitment to a social ontology has implications the form of epistemology deployed (Guba & Lincoln, 1994:108). That is, with states understood as being socially constituted, an approach premised on the accumulation of objectively identified knowledge is viewed as untenable as the social scientist is in fact confronted with a second order reality as actors inhabit a social world affected by social constructions of reality (Marsh & Furlong, 2002:19).

For this reason, constructivists typically deploy an interpretive epistemological approach to study. At base, this draws our attention to the importance of interpretation that is, establishing an understanding of that world. Eschewing the possibility of establishing causal relationships between phenomena, emphasis is instead placed upon providing a deeper understanding of what system we have, how it came about, and what opportunities exist within it for change or continuity (Schmidt, 2011:12; Marsh & Furlong, 2002:20).

Given the foregoing discussion, a constructivist approach rejects the view of institutions as self-reinforcing historical paths (historical institutionalism), all-defining cultural frames (sociological institutionalism), and static rule-following structures of incentives (rational choice approaches). Rather, arising in repudiation of what Blyth (2003:695) has termed their 'static bias', constructivist insights provide us with is a view of institutions as constraining structures and enabling constructs of meaning. That is, drawing on their 'background ideational abilities' (Schmidt, 2008:314), institutions are shown to be 'shaped by human action in such a way as to alter the parameters of subsequent action' (Hay, 2002:186), disposing its direction towards the achievement of outcomes operating to the advantage of certain actors at the expense of others. This is achieved through a dual process of conduct-shaping (direct power), and context-shaping (indirect power) (Nye Jr, 1990:180).

On the other hand however, the opportunity for contesting the context in which actors find themselves through processes of deliberation and contestation in order to communicate critically about institutions to bring about change (or more adequately affect continuity) is present in actors' 'foreground discursive abilities' (Schmidt, 2008:314; 2010). Here, actors, through a political project of 'strategic social construction' (Chwieroth & Sinclair, 2010:6) are able to, particularly during times of economic and/or political failure, re-shape the broader context of what is considered socially, politically, and economically possible.

The means by which these insights inform this research are explored hereon. In doing so, Schmidt's (2008) distinction between the coordinative discourse (how economic ideas are coordinated in a broader institutional context) and communicative discourse (the means by which they are legitimated and disseminated) is drawn upon to demonstrate the importance of power and position while taking into account the power of ideas. Thereafter, a discussion is undertaken regarding the role of crises in affecting change and continuity.

Coordinative discourse: Overcoming the materialist/ideational divide

The coordinative discourse (Schmidt, 2008, 2010) draws the attention of this research to the importance of the groups at the centre of policy construction who advocate a particular set of economic ideas – understood for the purposes of this research as assumptions regarding the appropriate form and function of the global economy. This is 'the substantive dimension of ideas and discourse' (Schmidt, 2010:3) provided by state leaders or apex policy forums who engage in the creation and maintenance of global economic governance institutions.

The concept of the coordinative discourse is especially useful in drawing our attention to the fact that the IMF does not function as a stand-alone actor, but rather operates as part of a broader architecture of global economic governance incorporating, among others, the Bank for International Settlements (BIS), the World Bank, and Financial Stability Board (FSB).

The G7/20 in particular however is shown throughout this research to be crucial in providing the economic ideas that act as a crucial roadmap with which to steer the course of global economic governance. Indeed, Blyth (2002:32) has suggested that the economic ideas held by such participants of how the world is put together are essential, as in their absence it would be impossible to act in the international political economy in any meaningful sense.

Guided by these economic ideas, the G7/20 exercises its power in a number of key ways. Firstly, it serves a 'directional function' by 'setting agendas for the wider governance machinery, and pushing general governance trajectories', (Baker, 2008:105-107) through statements/communiqués which emphasise broad principles shared by members. Secondly, it has the power of instigation in setting broad agendas for more specialist bodies such as the IMF and FSB. Finally, it exercises a power to endorse the findings of the technical reports produced by these bodies for which it relies on for specialist research (Baker, 2008:107-108)

Although economic ideas are often talked about as if they were one concept, this research follows the likes of Schmidt (2008) and Mehta (2011) in distinguishing between three levels of generality which allow global economic governance institutions to interpret and act in the international political economy: economic philosophies, problem definitions, and policy priorities. Economic philosophies, those most relevant to actors constituting the coordinative discourse, include ideas about how to understand the purpose of public policy in light of underlying, inter-subjectively held assumptions regarding the relative efficacy of states and markets in the functioning of the international political economy.

These ideas are crucial because they exercise a broad influence by determining the context within which actors find themselves. In doing so, they constitute the underlying, sometimes taken-for-granted assumptions that reside in the background of policy debates, providing the inter-subjective knowledge which creates the 'bubble' in which policy-makers act, and are rarely contested except during times of political and/or economic dislocation.

In this respect, economic philosophies play a critical role in constraining the normative range of solutions that can be viewed as politically acceptable or legitimate, concerned as they are, with broad-based attitudes and normative assumptions about what is desirable or otherwise within the broader confines of the coordinative discourse.

Following Campbell (1998:384) however, it is suggested that although some ideas are held as so taken-for-granted that they are invisible, the concept of an economic philosophy so understood for the purposes of this research is not as strong. Rather, it is interpreted here as having the potential to be visible to actors, yet taken-for-granted in the somewhat milder sense that they remain largely accepted and unquestioned background assumptions.

This concept is therefore crucial as, drawing on the constructivist premise that there exist multiple pathways by which to organise the international political economy, the notion of the economic philosophy provides us with an inter-subjectively held interpretive framework which, for the purposes of this research, implies a more or less shared condition among members of the nature of the efficacy of markets. Moreover, drawing on the economic philosophies held in the coordinative discourse, we are provided with an explanatory account of why political economic problems become identified as such.

That is, the notion of a narrowly-defined interpretive framework implies a drastic reduction of complexity to a small number of significantly articulated problems to be addressed. The corollary is that when they become so defined, 'a whole range of problems which could be logically associated with policy, will not be taken into account' (Jobert, 1989: 377) given their evacuation at an early stage by political-economic elites in the coordinative discourse.

Inasmuch as this is true, we can see how the economic philosophies held are critical in 'defining the problems to be solved... the issues to be considered; the goals to be achieved' (Schmidt, 2008:306). In performing this function, problem definitions constitute broad constraints 'on the range of solutions that actors perceive and deem useful for solving problems' (Campbell, 1998:389) because they have a major influence on the direction of subsequent action (Jobert, 1989:382). Problem definition effects are therefore profound precisely because they identify the nature of an issue and frame the context in which new events are interpreted; define the range of collective discourse on which problem definitions are bound; and guide decision-makers in the appropriate means to resolve them.

This approach therefore overcomes a weakness in existing literature which is biased towards ideas that ultimately contribute to policy, yet which in doing so, neglect the point that an absence of policies can also mean an inattention to other facets of (background) power because analysis is limited to what actually makes it onto the agenda. Yet by drawing attention to the importance of the underlying economic philosophy in the coordinative discourse and demonstrating how it impacts upon problem definitions, we are able to show why it is that some policies make it to the table while others are excluded (Mehta, 2011:31).

Following Schmidt (2010) and Blyth (2002) policies, problem definitions and economic philosophies are shown to exist, and be typically justified, at two levels of generality: cognitive (ideas justified in terms of interest based logics and necessity) and normative (ideas legitimated by their appeal to values and appropriateness). These can be given equal weighting, or alternatively, one or the other may be emphasised in the act of persuasion.

This research for example shows how the G7/20 is guided by, and concerned primarily with the purveyance of normative ideas, most notably a belief in the efficacy of free markets as opposed to an active state in managing the economy (Schmidt, 2011:6). That there is nothing inherent in their assumed efficacy to suggest that they are de facto correct however draws our attention to the fact that the normative ideas held by actors in the coordinative discourse are inherently political, particular to time and space, and socially contingent.

These ideas nevertheless play a critical function in attaching values to action in the political economy, legitimating economic philosophies through appeal to their appropriateness. In doing so, normative ideas speak to how policies mesh with underlying ideals, and how problem definitions resonate with the deeper economic philosophy, whether they be newly emerging or long-standing. Acknowledging this allows us to overcome a problem with much IPE literature which ‘tends to be more concerned with cognitive ideas that provide guidelines for political action... rather than on normative ideas that attach values to political action' (Schmidt, 2011:5; see also Schmidt, 2008:307).

Drawing on their common adherence to a particular economic philosophy and problem definitions, this research shows how the G7, along with other global economic governance institutions, propagate the coordination of a particular discourse – a set of assumptions regards the proper functioning of the global economy – to construct the broader context within which actors find themselves (Epstein, 2010:175; Broome & Seabrooke, 2012).

In doing so, the discourses held provide them 'with an interpretive framework, which describes and accounts for the workings of the economy by defining its constituent elements and "proper" (and therefore "improper") interrelations' (Blyth, 2002:11). As a result discourse, imbued with a cohesive set of economic ideas about how best to organise global governance, frame and de-limit the possibilities for action (Epstein, 2008:2). Indeed, it is within the confines of these 'normative parameters' (Baker, 2008:106) that politicians and policymakers are bound together, allowing them to interact and function socially.

The coordinative discourse is therefore crucial to this research in drawing attention to the constitutive nature of global economic governance by 'defining the set of practices that make up any particular consciously organized social activity – that is to say, they specify *what counts* as that activity' (Ruggie, 1998:22). Eschewing emphasis on antecedent actors and their behaviour, focus is placed on the way in which the economy is 'embedded in broader social, political, and legal institutional frameworks that make it possible to conduct economic relations – that are *constitutive of* economic relations' (Ruggie, 1998:23). As a result, the G7/20, IMF and others exist and exhibit important causal effects by influencing the direction of the international political economy as a socially constructed devices.

Inasmuch as this is true, the institutions of global economic governance are able to draw on their power and position, or 'background ideational abilities' (Schmidt, 2008, 2010) to shape the broader context of what is considered socially, politically, and economically possible. Understanding their role in such a manner helps us to overcome 'a tendency within the scholarship interested in the "social construction of" to evacuate power' (Epstein, 2008:8-9).

Rather, the preceding discussion demonstrates how material practices and the ideational and discursive realms are in fact 'tightly bound up and mutually constitutive' an assumption which 'moves the debate beyond a dichotomy carried over... from the old divide between ideationalist and materialist lines of explanation' (Epstein, 2008:5). That is, discourses have very real effects such that it makes no sense to consider them as "immaterial".

Although power is therefore key in this research, it is nevertheless understood for our purposes as residing in the capacity of actors in the coordinative discourse to produce predictability and order among actors within a socially structured community. Indeed, exercised effectively by actors, change is often very hard to enact (Hopf, 1998:180).

The communicative discourse: Shaping actor's interests

Just as the coordinative discourse is crucial in drawing our attention to the manner in which the economic ideas steering the course of global economic governance are produced, so too does Schmidt (2008, 2010, 2011, 2012) draw our attention to the importance of the manner in which they are communicated and disseminated through the communicative discourse.

Here, when speaking of the IMF in particular, we can see how it engages in such an endeavour through the production of Annual Reports, bi-annual World Economic Outlook and more specialist publications, the Global Financial Stability Report and Fiscal Monitor. These are themselves informed by a range of technical Working Papers, Staff Position Notes and Policy Papers and publications by IMF staff in high ranking economic journals.

These are subsequently distributed to, and are most read and cited by, member country authorities in policy discussions (particularly on macroeconomic issues), central banks, regulatory ministries, academia, businesses, think-tanks, the media, along with other international organizations (IEO, 2011:4; IEO, 2011a; 2011b:10-12).

The economic ideas developed here are further communicated and legitimated through conferences and seminars, the participants of which typically include representatives of other global economic governance institutions, senior government officials, central bankers, private market actors and senior academics. That the IMF is so heavily engaged in such a process is testament to the recognition that, absent communication, the impact of the coordinative discourse would be limited, and exhibit only a trivial effect on policymakers. The rationale for communicating a particular set of economic ideas to a larger audience is therefore simple, to contribute to the convergence of the prevailing economic philosophy, problem definitions, thereby forming the basis of new policy practices (Schmidt, 2008:310).

These premises are especially pertinent to this research. That is, given the severity of the financial and economic downturn, it would be insufficient from a constructivist perspective to simply state that economic ideas were characterised by continuity because doing so reflected the normative orientation of those actors constituting the coordinative discourse. Although this is of course a crucial part of the story, it is perhaps even more important that the discourse centring on the need for continuity be justified cognitively so as to persuade states that doing so was consistent with their interests, hence the importance of the IMF.

Therefore, while accepting the importance of the role of the communicative discourse, this research adds to the work of Schmidt (2008) in two respects. Firstly, it is suggested that the communicative discourse functions not simply as a communicative tool, but as a means by which to shape how actors perceive their interests. Secondly, we explore the means by which this is achieved, that is, through the production and dissemination of IMF research.

On the one hand, this research views interests as being less about structural determination and more about 'the construction of "wants" as mediated by beliefs and desires – that is, ideas' (Blyth, 2002:29), or more specifically for our purposes here, economic ideas (Blyth, 2003:702). Such interests are nevertheless "real" because actors act upon such under-standings and alter them as a result of those thoughts, and in this respect agents can be considered 'sentient' (Schmidt, 2010:7). Viewed in such a manner, following Abdelal et al (2005:29) interests are understood here as constituting the 'output side of construction'.

Although this is a general premise accepted by constructivists, they nevertheless differ over the means by which institutions instantiate ideas and interests, that is, which of the various 'input mechanisms' of social construction to deploy (Abdelal et al, 2005:29). Of these, three typically prevail: socialization, manipulation and persuasion, with each being influenced by the manner in which the world is viewed as hanging together and changing or continuing.

On the one hand, socialization draws on the notion that ideas spread evolutionarily through interactions with groups through decentralised and consensual processes of deliberation (Abdelal et al, 2005:33-35; Adler & Haas, 1992). On the other hand, manipulation suggests that ideas are imposed on others but that recipients "rationalise" them to the point that they are rarely questioned, ultimately becoming part of a socially-constructed landscape.

The approach taken to this research however draws on Schmidt (2010:17) who suggests that, 'change in interests can come from persuasion', that is, through the communicative discourse provided by the IMF. It suggests that economic ideas are brought into the political economy and states persuaded of their efficacy to such an extent that they alter the manner in which they perceive their interests, and ultimately, their behaviour (Schmidt, 2008). This suggests that actors relate to new ideas in a relatively conscious and/or internalised way.

To this however an important caveat is added. That is, in the act of persuading others of the benefits of a particular course of action this process has involved, on the part of the IMF, the evacuation of alternatives. Therefore, although the act of persuading is important, there is a need to acknowledge that the approach taken by the IMF is not entirely benign. Indeed, consistent with Epstein (2008:9) it is suggested that being persuaded can include 'having no choice but to talk (and act) in a certain way', because other ways have been actively evacuated, 'a possibility which is never really acknowledged in the emphasis on persuasion'.

On the other hand, if we accept that persuasion takes place, this leaves us with the question of how are actors persuaded that undertaking a particular course of action is in their interests? The answer is shown here as laying in large part on the role played by research.

It is here that the IMF plays a crucial role in the production of cognitive ideas which speak to the logic and necessity of economic philosophies 'as actors have to be persuaded to accept, or at least pay heed to, the arguments and messages' (Baker, 2008:108) developed by actors in the coordinative discourse. This is more likely if they are based on data and evidence as opposed to political exhortation. Indeed, senior staff have sought to distance themselves from this charge by touting the IMF as 'a neutral, expertise-based institution' (Best, 2003:363) which derives legitimacy from the production of apolitical technical knowledge.

In doing so, the IMF seeks to articulate cause-and-effect relationships, often citing numerical indicators as an important aspect of adding credibility to knowledge claims. Doing so, it is suggested, adds credence to attempts to limit the choices faced by actors by defining the range of problems to be addressed, a process which by its very nature 'has significant implications for the types of policy solutions that will seem desirable' (Mehta, 2011:27).

Indeed, once a problem definition and objectives are given, the context in which states identify their interests and pursue their policy preferences is defined. In this regard, we can see how the IMF is crucial in providing the cognitive justification required to articulate a particular set of policy priorities over the range of all of the available alternatives.

This approach overcomes a propensity 'to treat ideas and interests as radically different and unrelated concepts' (Blyth, 2002:17) by demonstrating how economic ideas and associated research plays a crucial part in leading states to (re)define how they perceive their interests. In doing so, an assertion is made, consistent with Adler and Bernstein (2005:301), that the most far-reaching effect of institutions – read here, the IMF - might not simply be to define problems, but more deeply, lead to 'the reproduction or transformation of identities and interests' on the basis of which the utility of particular policies are identified and pursued.

Drawing attention to the manner in which the IMF undertakes this activity allows us to go over and above the concept of 'power over' more closely associated with the coordinative discourse. Rather, the addition of 'power of', exercised in the communicative discourse, allows for influencing states in less direct ways. Taken together therefore, power is shown to be a disposition (in the sense of ordering) that depends on knowledge, and 'productive in the sense of defining the order of global things' (Adler & Bernstein, 2005:294).

This shows how control over knowledge is critical as the IMF calling a certain way to organize the political economy rational and optimal is a way of claiming power (Babb, 2012; Haas, 1992). That is, once a claim to rationality is accepted and experts deemed to speak the truth, the scope for alternative economic philosophies, problem definitions and thereby the kinds of policies considered desirable, becomes inherently limited (Kratochwil, 2001:19).

Doing so however both prevents actors from acquiring the critical analysis enabling them to separate ideas consistent or otherwise with their interests, and implies the communicative discourse is not as benign as that postulated by Schmidt (2008) who suggests that ideas are subject to complex processes of deliberation and/or contestation in an institutional context.

The approach taken here is therefore crucial in drawing our attention to the fact that many of the purported common sense knowledge claims derived from IMF research (subsequently iterated in the coordinative discourse) are in fact 'social/institutional facts' (Searle, 1995:6) collectively constructed within given institutional contexts (Schmidt, 2011; Palan, 2000). This demonstrates how 'knowledge systems cannot be transcendental and universally valid, but must be systems of power grounded in particular sets of social relations' (Amin & Palan, 2001:565), which for our purposes here, is provided by actors in the coordinative discourse.

A constructivist approach is therefore useful for the purposes of this research precisely because it 'concerns itself with the nature, origins, and functioning of social facts' (Ruggie, 1998:13) and in doing so, draws our attention to the fact that knowledge claims derived from dry, ostensibly apolitical IMF research are in fact grounded in broader normative parameters, existing in a particular time, and embodying particular values and interests.

Crucially therefore, by drawing attention to the contingent nature of economic ideas and the knowledge claims with which they are associated, constructivists point to the potential for agents to alter (or be in such a position as to maintain) the existing social, political and economic order through social action (Bevir & Trentman, 2004:5-19; Schmidt, 2010, 2011).

Taken together therefore a constructivist approach is crucial to this research precisely because it 'attempts to specify the macro-structural dimension of international politics in a manner that shows it to be space-time contingent: that is to say to make transparent the fact that "structure" is the aggregation of specific social practices that are situated in time and space; to specify what the characteristic forms of those practices are; and to discern how they may become susceptible to change' (Ruggie, 1998:26). This shows the importance of exploring how the economic ideas steering global economic governance become embedded; as well as the social/contingent nature of the knowledge claims they make.

Institutional and ideational change

The preceding discussion shows how the economic ideas steering the course of global governance, and their associated knowledge claims, are socially contingent and temporally bound. As a result, constructivist approaches have much to offer on the potential for actors to re-shape the context in which they find themselves. This overcomes the subordination of agency to structure by noting how institutions are constraining structures, and constructs created and subsequently changed (or maintained) by states. The question remains however, under what circumstances might we expect ideas and institutions to change?

Here, crises are typically held up as moments of great transformation. For rational choice approaches crises are viewed as exogenous shocks occurring as a result of, for example, a downturn in the business cycle, which agents automatically respond to in predictable ways.

Constructivists however suggest that crises are not given, and that agents do not react predictably to them and have therefore sought to endogenise the processes of change (Widmaier, 2005:557). In particular, attention has focused on how moments of political economic failure are inter-subjectively interpreted by actors *as* a crisis requiring decisive intervention to rid the system of its accumulated pathologies to effect change (Hay, 1999).

Understanding the concept of crisis in such a manner is crucial to this research. That is, by defining crisis as a moment of thorough-going change, a clear distinction is made between political-economic failure (the accumulation of contradictions which provide the conditions for crisis, yet which have the potential to result in transformed or un-transformed structures), and the moment of crisis in which agents inter-subjectively interpret such failure as requiring decisive intervention (change) (Thompson, 2009:137).

This literature related to failure, crisis and change is premised on a number of core themes. Firstly, that particularly during times of political economic failure, rather than the systemic context being characterised by risk, it is instead characterised by one of uncertainty.

Here, Knight (1958:233) defines uncertainty as a situation in which actors sample the past yet become even more wrong about the future since underlying dynamics invalidate our ability to draw conclusions from past behaviour; in particular, it is not possible to assign a specific probability to future outcomes because the situation is in a high degree unique.

Secondly, what actors' interests are (structural location will not tell us) has little meaning under uncertainty (Abdelal et al, 2005:15). Rather, interests must be defined in terms of the ideas actors have about the causes of the uncertainty they are facing 'precisely because they reduce uncertainty and give content to interests' (Blyth, 2001:3) by defining a moment of failure *as* a crisis and projecting the institutions that will ultimately resolve it.

Thirdly, the preceding two themes stress the importance of assigning meaning to events as it is only possible to react to crises once they have been interpreted through frameworks of understanding. Crises do not therefore dictate an obvious solution. Rather, moving from one set of ideas and institutions to another is an endogenous process (Blyth, 2002:8).

Crises are therefore not politically meaningful without processes of construction. As a result, building a narrative is a requisite for policy action as only by interpreting political-economic failure ('what went wrong?'), and proposing solutions ('what to do about it?') can policy-makers create the space for policy change. For this reason, 'much of the political argument is fought at the level of problem definition' (Mehta, 2011:27; see also Baker, 2015:344).

Key in this process in persuading actors of the benefits of a particular course of action is research which, in addition to helping instantiate a set of economic ideas, can similarly be used to bring about competition in ideas, and ultimately change, by exposing the inefficacy of existing ideas which were responsible for bringing about political-economic failure.

Indeed, drawing on new research apex policy forums postulate that new economic knowledge represents an advance over the old in terms of the prospects it offers for economic growth and development. Research therefore plays a crucial part in hastening the day when policy- makers might accept the desirability of alternative economic ideas by demonstrating the falsity of existing premises and efficacy of alternatives (Kreuger, 1997:1).

Why moments of political and economic failure do not necessarily lead to change

The preceding discussion demonstrates how constructivists have sought to endogenise crisis and change as a means by which to demonstrate how the social context shapes outcomes, that is, a shift from structural continuities and their effects on agents to a focus on what agents do and how they frame their actions, with particular attention paid to the moment in which one socially constructed order is replaced by another (Widmaier et al, 2007:752).

Nevertheless, it was suggested in the introduction to this research that economic ideas in the IMF are characterised by a considerable degree of continuity as opposed to change despite the evident failure of neoliberal economic ideas. It might not, therefore, be unreasonable to assume that 'rational choice's core concepts – equilibrium, transaction costs and path dependencies – focused on statics (why things did not change all that much)' (Blyth, 2003:695) are well placed to provide an explanatory account of why this is so.

In eschewing this approach however, an assumption is made that constructivism is in fact better placed to help us to understand the means by which the IMF has constructed the current downturn in such a manner that neoliberal economic ideas continue to be desirable from a normative perspective and necessary from a cognitive perspective. In doing so a simple assertion is made that if change occurs because actors successfully construct and frame moments of political economic failure as a crisis, then 'it follows naturally that, sometimes, the reasons things don't change is for the same reason' (Hope, 2011:10).

This assertion is entirely compatible with a constructivist approach whose central tenet is 'the social world, unlike the material world, is not "given" but rather socially constructed' (Epstein, 2008:6). Indeed, following Hacking (1999:6) we can see how the social order that presents its self at any one moment in time is the result of social construction, whether this ultimately presents its self as change or continuity, that is 'X need not have existed, or need not be as it is. X, or X as it is at present, is not determined by the nature of things; it is not inevitable'. This suggests that a constructivist approach leaves us well placed to explore the means by which continuity in economic ideas in the face of failure has been achieved.

Against this backdrop it is suggested that the moment of failure may lead to the destabilization of a given set of institutions and ideas, yet in doing so there exists the potential for a range of competing narratives of what went wrong (along with the requisite policy remedies). As a result, agents must 'argue over, diagnose, proselytize' before they can be suitably placed to take any meaningful action (Blyth, 2002:9; Broome et al, 2012:8).

Indeed, Blyth (2002:39) has suggested that during moments of failure ideas are deployed by actors as 'weapons' to de-legitimate existing ideas and bring about change. Nevertheless, it is important to acknowledge that proponents of existing ideas motivated by ensuring continuity are actively engaged in this debate and there is no logical reason to suggest that those motivated by change will be the winners in this ideological battle.

That this is the case is almost self-evident. However, what is missing from the constructivist literature is a sufficient account of how actors engage in such a process. In response, two related means are posited here which are crucial to this research, each of which, although clearly interrelated deal with a different 'pathway' to constructivism (Abdelal et al, 2010).

On the one hand, the IMF is shown, particularly during the first phase of the downturn, to have reasoned through historical analogy to compare unfolding events with others that have preceded them in order to reduce increasing *uncertainty.* On the other hand, the politics of framing as a means by which to imbue *meaning* to unravelling events in the political-economy is shown to have been especially prevalent as the downturn progressed.

Historical analogy

In the case of the former, it is suggested here that a key mechanism by which the IMF initially sought to construct continuity was through learning from history, a process by which policymakers look to similar instances from the past to help them deal more effectively with the uncertainty associated with seemingly novel problems in the present.

This is a process typically associated with International Relations and foreign policy analysis in particular. Here, the "Munich analogy" is most frequently invoked by policy-makers, typically as a means by which to justify military intervention, the assumption being that inaction leads to the kind of appeasement that led to the outbreak of World War Two.

The historical analogy literature is characterised by two distinct strands. On the one hand, the *analytical view* draws heavily on cognitive psychology to highlight the power of ideas as policymakers draw on historical analogies to make sense of current dilemmas, the conclusions of which influence the direction of policy decisions in the present.

This process has been summarised by Vertzberger (1986:225-227) who suggests that the use of history serves four broad functions. Firstly, it helps define a situation by interpreting information in order to construct a meaningful body of knowledge about the nature of the environment facing actors. Secondly, a circumscribing role is assigned to actors whose status is appropriate to that actor. Thirdly, a strategy is determined that defines the most effective range of policies for coping with events. Lastly, a justifying strategy is advocated to convince others that the proposed policies are logical, practical and normatively acceptable.

On the other hand, the *sceptics* eschew the analytical view's notion that history its self is a powerful determinant of policy. Rather, the sceptic view is instrumental and political. It suggests that policymakers draw on historical analogies to advance policies already decided upon. Schlesinger (1986:444) for example has observed that 'the past is an enormous grab bag with a prize for everybody', a view which 'diminishes the force of the argument that history is per se a powerful determinant of policy'. With this in mind, the sceptics deny that analogies serve a critical diagnostic role in helping to interpret incoming information, but rather serve a justificatory and advocacy, as opposed to analytical, function.

These differences notwithstanding, the two approaches have one pervasive similarity, with both acknowledging that more often than not, historical analogies are used badly. Analytical scholars for example observe that the cognitive approach 'prevents or delays recognition of the limits of validity of the lessons of history to current decision tasks', to such an extent that 'preference for information processing and decision-making by analogy, as well as an exaggerated perception or similitude between past events and present problems and information, are enhanced' (Vertzberger, 1986:234) thereby leading to suboptimal policies.

For the sceptics however, poor performance stems from the fact that analogies are selected as justificatory tools by policymakers for policies already decided upon at an earlier stage of the selection process. As a result, when resorting to historical analogy, they seize upon the first that comes to mind without stopping to analyse its fit or the manner in which it may be misleading, rather than searching for others that may be more appropriate (May, 1973:xi).

With the preceding discussion in mind, a key assumption of this research is that, although primarily the purveyance of IR, learning from the past has demonstrable utility in the study of the international political economy which is an incredibly complex and uncertain arena of interaction. For the purposes of this research it helps us understand the means by which the IMF attempted to deal with increasing uncertainty during the first phase of the downturn.

That is, it is suggested that the IMF, during a time of increasing uncertainty, interpreted incoming information through existing schemas and resorted to historical analogy to guide it through the indeterminacy of seemingly novel policy problems. In doing so, an attempt was made to posit uncertainty as more closely resembling a situation of risk which meant the broader environment was knowable and therefore resolvable in the frames of reference provided by the existing economic philosophy, problem definitions and policy priorities.

In explaining how this was so, this research draws on insights provided by the Analogical Explanation (AE) framework developed by Khong (1992:7-12) which synthesises insights derived from both the analytical and sceptic approaches. On the one hand, the AE frame-work suggests that we (either as individuals or collectives (Vertzberger, 1986:225)) have limited cognitive capacities, so to cope with vast amounts of information, resort to "knowledge structures" including schemas (a subjective theory about how the social/political/economic world works). These provide the necessary categories and labels which enable us to order, interpret, and simplify the world to make sense of our environment (see for example Larson, 1985:51). Indeed, Khong (1992:25) suggests that events in the world are never approached as if they were sui generis, but are assimilated into pre-existing structures due to limited cognitive capacities.

As a result, schemas help us to understand the origins, cuing, and function of historical analogies, a process by which new instances are matched to those stored in memory. In doing so, analogies play a diagnostic function by defining the nature of a problem by comparing the new situation with others from the past, and a prognostic function by forwarding policy solutions. This can be summarised thus: *AX:BX::AY:BY*. That is, event *A* resembles event *B* in having characteristic *X*. Given that *A* has characteristic *Y,* so is *BY* considered resolvable through the same policies deployed in event *A* (Khong, 1992:21).

On the other hand, the preceding discussion does not preclude the potential for historical analogies being used sub-optimally. This is so for three reasons. Firstly, there are systematic biases associated with schemas and analogical reasoning which means they are more often than not selected on the basis of surface similarities consistent with existing knowledge structures. As a result, other, potentially more appropriate analogies are often ignored. Secondly, once invoked, the default values of the schema/analogy fill in for incomplete information, thereby allowing for a fuller picture of events. Nevertheless, there is nothing inherent in doing so to suggest such information be applicable to that particular context. Thirdly, the result of the preceding discussion is that schemas/analogies often lead to perseverance as incoming information is incorporated into existing knowledge structures, with discrepant information slighted or ignored. As a result, they often persist as even in the face of contradictory evidence, and with their basic articles of faith unlikely to be eroded.

Finally, the AE approach does not deny the use of analogies for justification and advocacy. In fact, it allows for policymakers who are influenced by the lessons of history in arriving at them, but can be expected to use those same lessons to advance their policy preferences. Therefore, understanding the manner in which they are selected explains why analogies have the potential to play an instrumental role in persuading others of the relevance of the lessons learned in the policy process, and why their associated policy prescriptions are so often suboptimal in their application (Khong, 1992:13-17).

Taken together therefore, the approach outlined here provides this research with a perspective in which policymakers are shown to access analogies on the basis of surface similarities consistent with existing knowledge structures including schemas. This explains why similarities are highlighted and emphasised, while others that might contradict the analogy are ignored, and also helps us understand why this overall process can often lead to perseverance in economic philosophies, problem definitions, along with suboptimal policies.

The politics of framing

In the case of the latter, it has been suggested that the nature of political-economic failure is inherently contested, subject as it is to opposing tendencies or ‘persuasive struggles’ (Baker, 2015:344) as social agents seek to identify and remedy for paradigmatic and institutional anomalies created by a moment of failure through alternative diagnoses and prognoses.

The economic ideas held by those actors who prevail in such struggles are therefore keys to understanding why a particular outcome prevails at the expense of available alternatives (Blyth, 2001:2). From this we can discern that if experts educate power-holders about what problems exist and what the appropriate remedies are to them, moments of political-economic failure, constructed differently, means outcomes could have varied significantly.

Indeed, if interests are a function of beliefs and desires, and if agents are confused about those desires – particularly during periods of political-economic uncertainty, then it follows logically that their interests must likewise be unstable (Blyth, 2002:30). This leaves actors open to being persuaded of what course of action is in fact consistent with their interests.

There is therefore no a priori reason to be correct in assuming which actor or collection of actors might be successful in projecting a particular narrative of what went wrong and what is to be done. Indeed, engaged in persuasive struggles are not only various actors pushing for change, but also those motivated by ensuring the maintenance of the status quo.

In addition to historical analogy, actors also attempt to affect continuity through framing - the major premise of which is that 'an issue can be viewed from a variety of perspectives and can be construed as having implications for multiple values or considerations. Framing refers to the process by which people develop a particular conceptualization of an issue or reorient their thinking about an issue' (Chong & Druckman, 2007:104).

This concept has acquired considerable currency in the social sciences. References made to it, whether for descriptive or analytical purposes are increasingly found for example in such areas as psychology, linguistics and discourse analysis, communication and media studies, and political science and policy studies (Benford & Snow, 2000:611).

Nevertheless, the frame concept has arguably been explored nowhere as systematically than in sociology and most extensively to the substantive study of social movements and collective action where it has acquired substantial popularity, particularly from the 1990s. This research has taken as problematic what until this juncture had been largely ignored by structuralist/materialist concerns, that is, ‘meaning work – the struggle over the production of mobilizing and counter-mobilizing ideas and meanings’ (Benford & Snow, 2000:613).

In doing so the literature has become increasingly interpretive, ideational, and grounded in the assumption that ‘meaning is pivotal’ (Benford, 1997:409) given its centrality to issues related to construction, interpretation, attribution of blame/causality, the mobilization of support, and strategic interaction. Indeed, it has been suggested that ‘whatever else social movement actors do, they seek to affect interpretations of reality among various audiences’ (Benford, 1997:410), the assumption being that meaning acts as a crucial prefatory to action. In this regard, framing can be viewed as inherently constructivist (Steinberg, 1998).

Against this backdrop, two key insights are derived from this literature that informs this research. Firstly, frames – ‘the ability to define what the essence of a problem is’ (Cohn, 2013:114) - provide a critical *diagnostic* function by identifying, labelling and assigning meaning to occurrences in the international political economy. This process, commonly referred to as ‘frame amplification’ (Benford & Snow, 2000:623) involves accenting and highlighting particular problems, issues, events or beliefs as being more salient than others.

Moreover, frames help to foster agreement by promoting definitions and interpretations of issues in an effort to render particular problem definitions meaningful, and thereby function to organise expectations by simplifying and condensing aspects of the real world 'out there' (Chong & Druckman, 2007:106). As part of this process causal reasoning is key, particularly attributions of the root of the problem, inferences regarding the responsibility for treatment of the problem so-defined, as well as appeals to higher principles in the framing of an issue.

The diagnostic process therefore denotes what Benford and Snow (2000:614) refer to as ‘an active, processual phenomenon that implies agency and contention at the level of reality construction. It is active in the sense that something is being done, and processual in the sense of a dynamic, evolving process’. This agential emphasis draws attention to the fact that meaning is subject to differential interpretations, and therefore, the development, generation and elaboration of frames is a contentious process, with all actors in the political economic arena engaged in reality construction through the politics of signification.

The foregoing discussion implies that meaning is inherently contested, articulated and rearticulated to such an extent that it is not possible to simply construct and impose frames on their intended targets any one version of reality they would so wish (Benford, 1997:410). Rather, it is suggested here that successful frames – those that exert a considerable degree of influence over the manner in which problems are diagnosed and responded to - must be constructed in such a manner as to be persuasive: in cognitive terms by providing a compelling case of their necessity and efficacy; in normative terms by appealing to, and most closely coinciding with or seeming to protect, actors' underlying values; or a combination of the two to exert a particularly broad appeal (Chong & Druckman, 2007:111).

Secondly, framing plays a *prognostic* function, a process which involves, further to rendering problems meaningful and helping to foster agreement, organizing expectations which serve as important guides for action. This supports the premise that frames are constructed, by and large, to draw attention to a particular problem or situation that actors perceive as salient, make attributions regarding who or what is to blame, and thereafter articulate a set of arrangements in an attempt to affect change or continuity. This approach is consistent with the view that frames are both developed and deployed in such a manner as to achieve a specific purpose, that is, the advancement of a particular set of policy priorities.

In short, the prognostic function therefore addresses the question of what is to be done. Indeed, frames exist as a means by which to mobilize adherents, acquire broad support, and demobilise antagonists in the process, in order to push for a particular set of policy interventions to remedy the problem so-defined. Here, there tends to exist in reality a very close correspondence between the identification of the manner in which a particular problem was understood, and the constraining effects that this subsequently has on the kinds of responses that can be considered desirable. This involves articulating a proposed solution to the problem or at the very least a coherent plan of attack, and the required strategy for carrying out the plan (Benford & Snow, 2000:614-616; Pan & Kosicki, 1993:64).

The approach taken to this research is therefore critical in drawing our attention to the fact that frames are not naturally-occurring or objectively identifiable but are part of a strategic and deliberate activity that implies the use of agency in the construction of meaning. That is, interpretive frames are generated, and act to, identify the nature of problems by attributing causality, and identifying the remedies to those very problems (Benford & Snow, 2000:614).

Taken together, the two approaches discussed here, historical analogy and framing, demonstrate the importance of the economic ideas held by the IMF, and the means by which they are drawn upon and deployed to reduce uncertainty and assign meaning to events in order to push for continuity as opposed to change. This approach neither renders structure irrelevant, nor denies that agents have interests.

What it does do is draw our attention to the fact that under conditions of uncertainty (read here, political-economic failure), the politics of ideas is crucial as events do not simply and automatically telegraph to agents their true nature, they do not imbue in actors a mechanical sense of what should be done to remedy for their pathologies, nor do they dictate what course of action is in their best interests. That this is the case creates space in which the IMF is able to embody - and frame, shape, and embed what is legitimate and appropriate – the very ideas and rules, which are themselves contested to secure their propagation by attempting to re-affirm the rules of the game (Rueschemeyer, 2006:245).

In doing so, this research demonstrates how the IMF attempted to ensure that - even during ideological contestation – the frames established previously did not disappear.

Certainly, defending existing economic ideas is made easier as, although not impregnable, once the institutional power to discipline has been exercised, change is extremely difficult to enact. This suggests that 'corrected behaviour' (Kiersey, 2011:3) (change) need not be the natural corollary to the failure of institutions and their attendant ideas.

Adjudicating between change or continuity

Discussion has thus far concerned its self with the process by which continuity may be achieved. However, this leaves an important question as to by what means is continuity to be judged? Here, constructivists 'tend to divide between a crisis-driven view of policy change through 'paradigm-shifts' and more incremental approaches to policy change in ideas and discourse over time' (Schmidt, 2011:2). These tend to map out differently onto the three levels of generality discussed previously, policies, problem definitions, and economic philosophies. The approach taken here however suggests that the answer lies not in the policy realm, but in the ability of the IMF to continue to successfully project existing problem definitions, themselves a reflection of the broader economic philosophy.

Here an assumption is made that policies can be implemented in the context of failure that appear to run contrary to prevailing problem definitions and economic philosophies, thereby suggesting that existing policies have been usurped, have simply proven to be wrong, or are unable to deal with pressing problems. It is therefore policy ideas that change most rapidly as windows of opportunity open up in the face of events as old policies no longer solve the problems or fit the politics for which they were designed (Schmidt, 2011:5). The opening of a window – read an event or crisis – is mainly what drives policy change.

Nevertheless, policies that appear counter-intuitive to the prevailing economic philosophy and problem definitions may simply represent a means by which to shore up the existing system as opposed to being demonstrative of more substantive change. As a result, change in policies need not be indicative of a more significant shift in economic philosophy.

With this in mind, looking at the underlying economic philosophies and problem definitions are keys. Although premised on for example power and position, problem definitions typically exist during a particular time and place as they appear better able to define the problem of that time. This also explains why they change. Because they are less able to cope, or are *perceived* as being less able to cope with, changed realities.

As a result, problem definitions and economic philosophies exist for only a limited period of time, after which change comes from either internal or external processes or events which create a receptive environment for new ideas. So change often (although not exclusively) comes about at moments of great uncertainty when old institutions have failed and there is a perceived need for new ones. Here we would expect to see a radical shift in the policy sector to a new problem definition with different goals and broader economic philosophy.

In eschewing the notion however that as bad economic philosophies and problem definitions fail, good ideas take their place, an important part of continuity suggests that power (the ability to shape the broader institutional context through reference to discourses and narratives) has an inevitable part to play in this process. That is, change need not correspond directly to this changed reality as entrenched interests continue to fight for, and demonstrate, the efficacy of existing economic philosophies and problem definitions. How do we know therefore when we have institutional and ideational continuity? New circumstances are recognised and dealt with within existing problem definitions.

Concluding remarks

This chapter has advocated a constructivist approach as a means by which to account for the manner in which economic ideas become instantiated in institutions, and what opportunities exist for change or continuity in the context of crisis. Doing so has allowed for a deeper exploration of two areas key to this research, the relationship between the material and ideational realms, and the relationship between crisis and change/continuity.

Firstly, it has been suggested that the co-constitutive relationship between context and agency (represented here as the coordinative and communicative discourses) provide both the broader setting within which events occur and acquire meaning, yet which present multiple branching points and potentially divergent courses of action.

Secondly, the importance of the role of ideas has served the purpose of demonstrating not only the importance of ideational analysis in political economy scholarship, but its relevance in particular upon 'the ideological face of governance' which 'needs to be understood as constituting the very fabric of the picture we are trying to build up' (Payne, 2005:72). That is, global economic governance is predicated upon a particular economic philosophy composed of an accompanying set of problem definitions and policy priorities.

Thirdly, drawing on the discussion on crises, three points can be made that inform this research. Firstly, a constructivist approach has been shown to open up space in which 'ideas can contest and de-legitimate existing institutions and patterns of distribution' (Blyth, 2001:2) during times of political-economic failure in order to effect change.

Secondly, the postulated need for change is liable to be subject to contestation from entrenched interests which seek the perpetuation of status quo institutions and ideas. As a result, regardless of the severity of the perceived political-economic failure, there is no a priori reason why one set of economic ideas should win out over the other.

Finally, before agents can respond to a crisis they have to have some idea of what caused it (Baker, 2012:7). The role of the G7/IMF in particular have been shown to be crucial here, acting as agents for continuity through the coordinative discourse (by framing the problems presented by political-economic failure and the means by which it is to be resolved), and through the communicative discourse, (the dissemination of these very ideas).

Chapter 2

The IMF in historical context

It was not Keynesianism it's self, 'but the existence of exceptionally favourable conditions for growth that was responsible for the generally good economic record of the 1950 and 1960s' (IMF Annual Report, 1980:34)

Introduction

This chapter situates the IMF in its historical context. In doing so, three purposes are served. On the one hand, it charts the creation and initial remit of the IMF, underpinning which were Keynesian economic ideas which afforded government scope to intervene into domestic economies to foster growth and employment. Thereafter, it is demonstrated how the inflationary and growth crisis of the 1970s ultimately presaged a shift to neoliberal economic ideas given that Keynesianism was not only viewed as a crucial precipitating cause of the crisis but was, correspondingly, deemed incapable of remedying for its pathologies.

On the other hand, it is demonstrated with reference to the Latin American debt crisis and Asian Financial Crisis (AFC) how IMF policy responses have been underscored by neoliberal economic ideas. In doing so, the IMF has assumed a greater role in stabilizing economies affected by crises than had been the case under the BWS, by insisting on structural adjustment measures in order to redress the un-sustainable policies that led to the crises.

Finally, it is demonstrated how, despite its often dubious record, the IMF nevertheless continues to defer to the neoliberal economic philosophy, problem definitions and policy priorities in its crisis resolution strategy. Indeed, it is suggested that the IMF has, if anything, sought to further entrench reform in a range of domestic political and economic institutions. This is explored with reference to Financial Sector Assessment Policies (FSAPs).

Economic ideas I: The Bretton Woods System and Keynesianism

The competitive devaluation of currencies and exchange and trade restrictions that characterised the 1930s, along with the end of World War Two, proved motivating factors behind the creation of the Bretton Woods Institutions (the International Bank for Reconstruction and Development (IBRD) (now World Bank) and IMF (IMF, 2011:1).

Although in its initial incarnation the IMF was to be controlled by its member countries, the discourse surrounding the need for more effective multilateral cooperation was coordinated by the US under the leadership of Harry Dexter White, and the UK under the leadership of John Maynard Keynes who, upon their combined economic, military, and ideological dominance controlled almost half of all contributory quotas (Sutherland, 2014:3).

However, the nature of events in the inter-war years in and of themselves, did not materially telegraph to agents the form and function that cooperation should take. Rather, Blyth (2002:40) draws our attention to the fact that 'it is cognitively impossible for agents to construct economic institutions without having an idea as to what caused a given crisis', in this case, what policymakers thought the lessons of the inter-war years had taught them.

Although this demonstrates how 'all forms and projects of governance are intrinsically ideological' (Phillips & Payne, 2014:3) which in its self suggests that the initial remit of the IMF could have been radically different (had the lessons of the causes of the inter-war years been interpreted and diagnosed differently), governments signing up to the founding Articles were nevertheless guided by an inter-subjectively held consensus of the inefficacy of the economic philosophy, problem definitions, and policies of the inter-war years.

Governments signing up to the founding Articles of Agreement (1944) were therefore driven by a collective desire to avoid financial crises, disputed commerce, wild exchange-rate movements and political instability. The IMF therefore acted as protector of the global capitalist economy, promoting international trade and overseeing the international monetary system, yet allowed for domestic intervention to spread the risks of adjustment.

Against this backdrop, six objectives were prescribed in the IMFs Articles: (1) to promote international cooperation on monetary issues; (2) to facilitate international trade; (3) to promote exchange stability; (4) to eliminate exchange restrictions; (5) to provide loans to prevent members from resorting to measures destructive of national and/or international prosperity; and (6) to reduce the duration/magnitude of payment imbalances (IMF, 1984:2).

In doing so, the Bretton Woods System (BWS) required members to peg their exchange rates to the US dollar (which in turn was pegged to gold). Although there was leeway - one percent either side of parity - pegged exchange rates could only be adjusted on a proposal by the member, after consultation with the IMF, and to correct fundamental disequilibrium.

Moreover, it was to provide members with financial resources to enable them to observe the code of conduct while correcting or avoiding payments imbalances. This was premised on the assumption that although fixed exchange rates provided a considerable degree of day-to-day certainty their rigidity made participating countries susceptible to balance-of-payments deficits and/or crises (often referred to as currency crises) (Babb, 2007:131).

For classical liberal economists the need to restore balance-of-payments parlance typically involved a period of austerity and living within diminished means. Eschewing this approach however, the IMF - informed by Keynesian macroeconomics which legitimated domestic intervention during such times - was guided by an assumption that markets alone were unable to bring an economy out of a slump. As a result, the IMF loaned money short-term to correct maladjustments without members resorting to measures inconsistent with the code of conduct (destructive of national prosperity) to dampen cyclical fluctuations and foster the consumption required for economic growth and full-employment (Babb, 2007).

The Keynesian economic philosophy underpinning IMF policy advice therefore exhibited a clear commitment to an active state in managing the economy. This reflected a broad consensus that 'the prosperity of nations – in particular their levels of production and employment – did not need to be the unplanned outcome of an uncoordinated and erratic system but could instead be controlled by government' (Stewart, 1987:465).

This had clear implications for the manner in which economic problems were interpreted and responded to, and the kinds of policies considered appropriate. On the one hand, the IMF exhibited a clear commitment to the pursuit of economic growth and full employment while on the other hand this opened up the potential for the kinds of policies inconceivable by liberal economists, that is, the deployment of fiscal stimulus and deficit spending.

Economic ideas II: The decline of the Bretton Woods System and shift to neoliberalism

Although not attributable solely to the IMF, it nevertheless presided over a golden age for the global economy in the 1950s and 1960s characterised by sustained economic growth, generally low inflation rates, and the liberalization of world trade in goods and services which grew with the renaissance of cooperation engendered by the IMF (Bird, 2007:686).

However, from the late 1960s signs of strain which would presage the demise of the BWS and Keynesian economic ideas steering global economic governance, were increasingly evident. Firstly, the Keynesian assumption that financial markets could not maintain a stable equilibrium provided a normative framework in the IMF in which capital was controlled.

However, the creation of the Eurodollar market in the UK in the mid-1950s created an environment in which financial assets denominated in foreign currencies could be traded. This challenged the BWS in which central banks controlled exchange rates, something they could do only if they controlled capital flows (in the short-term).

This process was deliberate, and therefore neither inevitable nor inexorable (Abdelal, 2008). Indeed, Blyth (2003:3) draws our attention to the fact that it was the 'regulatory permissiveness' of key members (UK and US) as opposed to structural imperatives that weakened existing regulations by providing borrowers and lenders with alternatives to national regulation, the outcome of which was a shift to liberalized capital markets.

Secondly, devaluations of the pound sterling (1967), the French franc (1969), the floating of the deutsche mark (1971) and a new pattern of exchange rates with wider margins agreed in December 1971, according to the IMF Annual Report (1972), removed a foundation stone of the BWS and replaced it with a system in which countries would increasingly come to rely on foreign exchange markets to determine their currency values.

In doing so, the end of the BWS in 1973 precipitated a shift in the IMF towards principles that would guide members in the conduct of their exchange rate policies, the final details of which were incorporated into the Second Amendment of the Articles of Agreement (1978). These eliminated the role of gold and legalised existing exchange practices. It gave members the right to adopt exchange arrangements of their choice while placing certain obligations on them, over which the IMF was given extra surveillance power, the argument being that, since exchange rates would be determined in the market the Fund needed to monitor not only exchange rate policy, but also other domestic policies affecting those rates (You, 2005).

Thirdly and perhaps most pertinently for our purposes here, the Keynesian economic ideas underpinning IMF problem definitions and policy priorities were showing signs of strain, manifest in 'the continuation of rapid and widespread inflation', along with 'a deceleration in overall growth of real GNP' (IMF, 1970:4), commonly referred to as stagflation.

Indeed such was its persistence that by 1972 the IMF Annual Report noted that advanced countries 'must endeavour to control inflation while at the same time achieving satisfying levels of employment and rates of economic growth' (IMF, 1972:1). Although stressing the need to control inflation, the IMF therefore continued to defer to the Keynesian economic philosophy with economic growth and full employment retaining primacy as policy goals.

By 1974 however it was noted how stagflation contributed to 'the most complex and serious set of economic problems to confront national governments... since the end of World War 2', and thereby 'brought into focus the need for countries – especially the largest ones – to pursue a strategy to curb inflation before it leads to prolonged damage' (IMF, 1974:1).

Against this backdrop an assumption was made that tackling inflation would require an alternative set of economic ideas to Keynesianism which had 'tended to shade policy risks on the side of growth and employment' (IMF, 1974:10) beyond a point that could now be considered prudent. In doing so it was noted that policy decisions 'must now place more emphasis on controlling inflation and maintaining a climate of financial stability; despite the correspondingly lower emphasis on growth and employment objectives' (IMF, 1974:10).

Indeed, 'obliged to re-examine postulates that they had taken for granted in the 1950s and 1960s' (IMF, 1980:34) there was a crucial shift away from the Keynesian focus on growth and employment, to an almost exclusive focus on inflation targeting. Little attention was therefore placed upon the kinds of policies advocated in the post-war context which were understood to have been fundamentally discredited by the inflation and growth crisis.

Moreover, the IMF went even further than stating that Keynesian economic ideas were incapable of dealing with prevailing economic problems by suggesting that they were in fact a major precipitating cause of the very conditions facing policymakers. Indeed, the 1980 IMF Annual Report (IMF, 1980:34) suggested that although Keynesianism had seemingly provided a climate of stable growth, employment and good price performance, this was not Keynesianism its self 'but the existence of exceptionally favourable conditions for growth that was responsible for the generally good economic record of the 1950 and 1960s'.

With this in mind, although two oil shocks in the 1970s had contributed significantly to inflationary pressures, the preceding discussion shows how stagflation was nonetheless interpreted not as a crisis *for* Keynesianism, but more pertinently, a crisis *of* Keynesianism its self and the problem definitions and policy priorities with which it was associated. This claim was however supported by a plethora of IMF research which, according to former IMF Deputy Director Anne Kreuger (2005:2), brought about advances in our understanding of the inefficacy of Keynesianism and the pressing need to reorient economic ideas.

On the one hand, state intervention was increasingly viewed as problematic as it 'led to poor choices on capital movement, disastrously high concentrations of income, degradation of the natural environment, corruption, and ultimately, financial ruin' (Boughton, 2001:33). The Keynesian emphasis on fiscal policy was however, subject to particular criticism on the grounds that: it was overly ambitious and had destabilising effects as distortionary measures were enacted too late; measures were based on faulty economic forecasts; and consumers and businesses had learned to anticipate policy changes and therefore adapt accordingly.

On the other hand, inflation increasingly came to be seen as the result of rapid growth in a government's spending and full employment policies. An assumption was therefore made that financing government spending by increasing the quantity of money contributes to inflation, thereby making it a strictly monetary phenomenon. This meant that possible cures were limited. Indeed the solution was evident to those in the IMF, government would need to be taken out of running the economy and inflation would have to be tackled.

We can therefore see how, just as the Keynesian economic philosophy involved explicit assumptions regarding the proper role of the state in managing the economy, so too did Krueger (1997:2) suggest that a shift to inflation targeting could not be disentangled from a reconsideration of the role of the state, the circumstances for which, it was suggested, were increasingly favourable given the bad economics and politics that characterised the 1970s.

The preceding discussion notwithstanding, there was nothing inherent in the broader economy to suggest a problem inherent to Keynesianism, although political-economic failure at the time certainly contributed to an environment which increased the chances of it being construed as such. Nevertheless, Chwieroth (2010:496) draws our attention to the fact that moments of failure 'no matter how visible or severe, do not induce an automatic response'. Therefore, while rising inflation and declining growth offered a reasonable proxy for declining economic performance, what this means to each actor can vary considerably, depending on what each considers sustainable, and this comes with no obvious metric.

The point here is that these "facts" were not self-apparent phenomena that unambiguously telegraphed to agents what to do (Abdelal et al, 2010:10). Rather, what the apparent failure of Keynesian economic ideas and institutions did do was allow the IMF to construct a crisis narrative highlighting the declining performance of extant economic ideas, institutions and policies as a crisis *of* the status quo (particularly an over-extended state) requiring change. This draws our attention to the fact that the shift to neoliberalism 'was not economically given, but politically orchestrated' (Hay, 2010:1). Nevertheless, two factors contributed towards a particularly receptive environment for the success of this crisis narrative.

Firstly, the IMF was increasingly guided by a coordinative discourse driven by the G7, a group formed in 1976 by the world's leading economies (US, UK, Japan, Germany, France, Italy and Canada). This group, increasingly controlling IMF business, was formed as a result of: declining US hegemony and the need to multilaterally manage the global economy; a desire to exert political leadership; and the breakdown of the BWS (Payne, 2008:520).

The G7 therefore came to play an overarching role in relation to formal global governance institutions (including the IMF) by seeking to coordinate, prioritise, and steer policy actions (Payne, 2008:525). Indeed, it was at the very first meeting in Rambouillet that the members agreed the underlying principles of the post-Bretton Woods regime of market determined exchange rates and changed the IMF's Articles of Agreement (Baker and Carey, 2014:89).

Most pertinently however, the economic ideas guiding G7 problem definitions and policy priorities were consistent with the neoliberal economic philosophy. The first Communique of the then G6 in 1975 for example, without directly referencing the efficacy of the market, nevertheless spoke in terms consistent with this approach. This, although highlighting the need for economic growth and employment, included 'shared beliefs' of the need to 'avoid unleashing additional inflationary forces' which might threaten the economic recovery (G6, 1975:1). Indeed, the G7 Communique of the following year went even further, calling for fiscal restraint by speaking of the need for 'a restoration of a better balance in public finances as well as of disciplined measures in the fiscal area' (G7, 1976:1).

Secondly, the IMF was increasingly influenced by the 'formalist revolution' in economics in the 1950s in which mathematical techniques assumed greater significance. During this time the technical apparatus associated with neoclassical economics became dominant, a key contribution of which was to abstract economic questions in order to generate workable models free from social specificities, and in doing so, hollow out of the self reflexivity of Keynesian social purpose which had stressed the inter-subjectivity of economic activity.

This process involved a triple reductionism which 'remain today the bread and butter of neoliberal economic theory and practice' (Best, 2004:386) in the IMF. The first involved the reductionism to the individual and optimizing behaviour as opposed to collective agents, the consequence of which was an economy treated as an aggregation of individual elements. Secondly the economy is treated as if it were confined to market supply and demand absent non-economic factors. Thirdly analysis is based on the marginalization of historic specificity.

These insights provided the grounding for two hypotheses that – although never intended as a literal description of how people actually behave – nevertheless increasingly came to inform economic ideas in the IMF. On the one hand the rational expectations hypothesis assumes the presence of rational actors maximising their utility in complete and perfect markets. This assumption rested on two premises. Firstly, in forming their expectations rational actors make efficient use of all information available to them, although potential random shocks - not part of anyone's information - means that actors will behave consistent with the model only on average. Secondly, the model of the economy used by individuals in making their forecasts is the correct one – that is, the economy behaves in ways predicted by the model which we know is correct because they are subject to Darwinian processes of learning whereby inferior models disproved by events are weeded out (Skidelsky, 2009:34).

These two insights (the efficient use of information and stability) give the required amount of information and predictability to make expectations converge on average. That is, 'if all agents share the same model of the economy, and if there are no large informational asymmetries, then agents' expectations about possible future states of the economy should converge and promote a stable and self-enforcing equilibrium' (Blyth, 2002a:8).

On the other hand, the rational expectations hypothesis is transformed into efficient markets hypothesis which acknowledges that although the future is characterised by risk, it is nevertheless probabilistically measurable, and as a result share prices are always correctly priced, with only unpredictable shocks causing prices to differ from their 'intrinsic' values. This hypothesis 'came to be regarded as a state-space description of actual markets' (Blyth, 2012:10) from which it was deduced that: market prices are good indicators of rationally evaluated economic value; the risk characteristics of financial markets can be inferred from mathematical analysis; market discipline is an effective tool in constraining harmful risk-taking; and innovation is beneficial since competition weeds out those not delivering value (Blyth, 2012; Skidelsky, 2009:38-39).

Taken together therefore, the 1970s can be understood as a period in which the IMF under-went a major transformation in the economic ideas steering global economic governance. That is, a shift in economic philosophy from Keynesianism to neoliberalism (from state intervention to a largely 'hands-off' approach), in the manner economic problems were interpreted and goals pursued (from growth and employment to inflation targeting), and policies considered desirable (from fiscal interventions to controlling the supply of money).

Nevertheless, throughout the decade, the IMF became increasingly marginalised due to: members borrowing from commercial banks eager to recycle surplus oil dollars (Woods, 2006:7); and as the shift to floating exchange rates which diminished the Fund's role as the guarantor of exchange rate stability and regulator of global liquidity (Bird, 1999:955). However, underpinned by a neoliberal economic philosophy and drawn back into significant lending beginning with the debt crisis of the 1980s a new era was beckoning for the IMF.

Neoliberalism in practice I: developing country debt crisis

The lending generated by surplus OPEC dollars requiring recycling by Western banks ended when the US Federal Reserve increased interest rates in 1979 to address inflationary pressures. Borrowers in Latin America, beginning with Mexico in 1982 left several large banks facing failure, leading them to increase spreads and reduce the availability of credit.

The range and diversity of creditors involved made it unlikely that the crisis would, or could, be resolved without the active involvement of an outside agent. The IMF was therefore called upon to coordinate and make loans to debtors to ensure that they would be in such a position as to repay their over-exposed credit, and thereby, avert a global banking crisis.

The IMF, traditionally lender of last resort now found its self, given the drying up of private credit, as negotiator of first resort. Accordingly, loans were made with strict conditionality ('the policies a member is expected to follow in order to secure access to the resources of the Fund' (Buira, 2003:3)) an arrangement increasingly associated with IMF loans.

Guided by a neoliberal economic philosophy the IMF viewed problems presented by the Latin American crisis, and the requisite remedies to them, through an alternative analytical lens. In doing so, the crisis was considered different, and more serious, than the balance of payments crises preceding it and would require an alternative set of policy interventions.

Underscoring this shift was the concept of un-sustainability. According to the IMFs Articles members are only permitted to borrow when there is a balance-of-payments *need*, although because this is never defined, the concept *sustainability* is often deployed (which is of course entirely subjective). In an attempt to offer clarity, Bird (2007:696) suggests that a country’s balance-of-payments is unsustainable when current policies cannot be continued indefinitely and that major policy change is required. This is not solely indicated by a current account deficit, but also depends on a country's willingness to borrow and creditors to lend.

Viewed through the lens of un-sustainability, an assumption was made within the IMF that domestic mismanagement and bad policies (fiscal expansion, exchange rate overvaluation and foreign borrowing by governments) were the cause of payments problems, effectively something more severe than the short-term balance-of-payments problems with which the IMF was traditionally associated (Pastor Jr, 1989; Wade & Veneroso, 1998; Weisner, 1985).

This enhanced the IMFs case for lending based on a greater number of conditions which duly rose fifty percent (You, 2005:220). Therefore although limited to matters of macro-economics such as a government’s budget deficit, monetary policy, and inflation rate, the IMF started to suggest that since almost any structural issue could impact the overall performance of the economy, almost everything fell within its domain (Stiglitz, 2002:14).

As a result, policy programmes were not simply limited to stabilization (measures to remove inflation/fiscal gaps) through reduced government expenditure/investment; but included adjustment (creating the conditions for growth) such as the elimination of subsidies, based on the assumption that stabilization alone was futile if underlying problems remained.

Given the perceived un-sustainability of policies pursued by countries approaching the IMF, focus initially centred on stabilization to prevent balance-of-payments crises from spiralling further out of control. Policies included fiscal and monetary performance criteria (similar to adjustment under the gold standard), the aim being to promote economic balance in order to attain ‘a viable payments position in a context of reasonable price and exchange rate stability’ and ‘a sustainable level... of economic activity’ (Boughton, 2001:557).

Although aimed at preventing intensifying capital flight and soaring debt servicing burdens, key here, and assuming increased prominence in IMF programmes, was a commitment to maintaining the integrity of the price mechanism. Although the importance of price stability was recognised as early as 1959 by IMF Managing Director Per Jacobsson (1959:22) who stated that ‘sound economic development is not compatible with the distortions that rapid or chronic inflation always creates’, it has been shown here how it was not until after the stagflation of the 1970s that it assumed primacy as the key problem facing policymakers.

Against this backdrop, the IMF advocated a series of adjustment policies to Latin America including: reduction of fiscal deficits; currency devaluations to make exports competitive; eliminating protectionism and restraints on foreign investment; privatization to generate more productive enterprise and reduce the public payroll; reduced public spending to meet debt repayment obligations; the elimination of subsidies and government interferences; decreases in real wages by freezing public sector wages; and the abolition of price controls (such as in electricity or gas) to promote competition and efficiency (Abdel-Kander, 2013:1).

IMF programmes therefore came to be judged on the ability of governments to carve out a greater space for the market, premised on the neoliberal economic philosophy which made explicit assumptions that the market provided *the* model for efficiently managing scarce resources. Therefore, helping governments develop markets through privatization, trade liberalization, banking system restructuring and state spending restructuring increasingly constituted an important part of the IMF's work (Krueger, 1999a:4-5; Fischer, 1999:25).

Countries only approach the IMF for assistance during a crisis, so it is difficult to determine how successful (or not) they would have been in re-dressing an economic downturn in the absence of support. However, most indicators suggest that IMF programmes during the debt crisis were unsuccessful to such an extent that Pastor Jr (1989:80) suggested 'the IMF may be politically exhausted as a vehicle for crisis resolution and economic restructuring'.

This conclusion was based on the fact that: growth rates plummeted from 5.8 percent on average between 1968 and 1980 by about half during the years IMF policies were adopted; inflation did not even start to decrease in the region until late 1985 thanks to the growing adoption of heterodox programmes, which were often deployed against IMF advice; living standards fell dramatically in light of IMF interventions; external debt almost doubled between 1981 and 1987; and per capita income growth was negative/close to zero between 1982 and 1987 (Kreuger, 1999:1; Lustig, 1995:4; Pastor Jr., 1989:80-97; Rodrik, 1999:1).

Moreover, evidence pointed towards important asymmetric distributional consequences. Here, Pastor Jr. (1989:97) noted that it would have been reasonable to expect, given their part in hastening the crisis, that bankers should have borne a large share of the adjustment burden. Nevertheless, Rodrik (1999:1) noted how reforms in fact weakened social insurance institutions, employment was less secure and public safety nets were weakened, all in the name of ensuring the financing of debt burdens and ensuring the solvency of banks.

Programmes were therefore associated with significant declines in the real wage and labour share, with the urban poor and working class particularly affected by subsidy cuts, real wage reduction and price increases due to devaluations and the elimination of public services. The net result was, in most countries, the income share of the top ten percent increased, often substantially, while that of the bottom ten percent declined (Lustig, 1995:4). This led Pastor Jr. (1989:100) to suggest class favouritism in the IMF as crisis costs were socialised, a dis-proportionate amount of which was borne by those at the low end of the income spectrum.

Two broad conclusions can be drawn from the preceding discussion. On the one hand, advocating a reduction in fiscal deficits, decreases in real wages, and greater trade and capital liberalization was problematic under benign economic conditions but were an especially reckless set of pro-cyclical policies during a global economic slowdown.

On the other hand, the crisis drew attention to the fact that finance is characterised by a phase of over-lending in which banks aggressively seek new clients in order to protect their market share. Thereafter, banks collectively retreat from the market in a panic. This was a scenario envisaged by Keynes and was a key assumption informing economic ideas in the IMF in the post-war period which advocated the deployment of capital controls.

This called into question the justification for capital liberalization which had been advocated by the IMF as a key component of the Latin American growth strategy. However rather than the beneficent view of capital flows from advanced economies financing development, the pattern was directly reversed as capital flows were shown to be inherently pro-cyclical with the "basic transfer" (net inflows of capital minus interest payments) becoming negative, sinking from a peak inflow of $26.4 billion in 1981 to an outflow of $34.7 billion in 1985 (Pastor Jr., 1989:94), thereby making new loans necessary for investment difficult to obtain.

Financial sector liberalization and neoliberalism in practice II: Asian Financial Crisis

Despite the Latin American debt crisis pointing to the negative consequences associated with financial liberalization and deregulation it nevertheless came to develop an inextricable synonymy with IMF policy discourse. Its necessity was constructed upon efficiency grounds which posit that competitive markets yield efficient equilibria (Argitis & Pitelis, 2008:2). This view is consistent with the belief that regulations are, by contrast, responsible for distorting competitive markets, thereby causing them to deviate from an otherwise efficient path.

Then Managing Director of the IMF Michel Camdessus (1997:1) summarised the benefits of liberalized global financial markets, suggesting that they: 'give countries new opportunities to quicken the pace of investment, job creation, and growth; give investors a wider range of investment opportunities and higher returns on savings; and promote a more efficient allocation of resources worldwide and thus, contribute towards stronger world growth'.

It was against this backdrop that, from the 1980s and particularly in the 1990s, capital controls, once part of economic orthodoxy, were increasingly viewed as economic heresy as the belief that the free movement of capital was desirable (what Chwieroth (2010:1) referred to as 'the norm of capital freedom' within the IMF), became the new orthodoxy.

Although the role of capital mobility in particular was subject to contestation within the IMF - broadly delineated as it was, between gradualists who argued for sequenced liberalization and big bang advocates who sought rapid liberalization – differences were generally played out over the appropriate speed and nature of liberalization, not its inherent value.

Indeed, so entrenched did the assumed efficacy of financial liberalization become, that in 1997 the IMF's Interim Committee called for an amendment to the Articles to enable the IMF to promote the liberalization of capital markets, as well as give it greater jurisdiction over the capital account policies of member states. This shows how the IMF was not simply seeking to regulate an extant activity, but more fundamentally seeking to play a constitutive role in shaping a particular form of financial sector liberalization and de-regulation. That is, the IMF did more than simply analyse and respond to market forces, it attempted to fundamentally alter them: to paraphrase MacKenzie (2006:12) it was 'an 'engine'... an active force in transforming its environment, not a camera passively recording it'.

Paradoxically however, at the same time the IMF was attempting to do so, the volatility with which financial sector liberalization and de-regulation was increasingly associated was creating new forms of financial and economic crises originating from the impact of capital as opposed to the current account including those in Mexico, Russia, Brazil and Turkey.

Common to all was an initial liberalisation (encouraged in large part by the IMF (Radelet & Sachs, 2000; Stiglitz, 2002) which permitted substantial inflows of short-term investment. Indeed, empirical evidence demonstrated that after premature financial liberalization, countries were particularly vulnerable to rapidly expanding capital flows and their abrupt reversals, a problem aggravated by fragile domestic financial structures and weak financial regulation and supervision, a process exemplified by the Asian Financial Crisis (AFC).

Asian Financial Crisis

In 1997 a financial crisis hit a number of the world's most rapidly growing economies in Asia, resulting in some of the largest financial bailouts in history, yet was entirely unanticipated. Indeed in affected countries macroeconomic management was good, 'with generally prudent fiscal policies and high private savings rates, these countries had become a model for many others' (Karunatilleka, 1999:1). IMF Managing Director Michel Camdessus (1997:2) for example observed that 'the regions economic success over the last couple of decades can be described in many ways – as outstanding, superlative, and certainly admirable. But it was no miracle. Rather, it was the result of good policies'. There were therefore few signs of crisis, rather, bank lending actually rose to record levels in 1997 (Wade & Veneroso, 1998:1).

This success was premised, in part, on financial deregulation which encouraged private capital inflows; indeed in the run-up to the crisis the IMF recommended greater openness to such money which could finance investment half as cheap as it could domestically (Radelet & Sachs, 2000:122). Against this backdrop governments relaxed control on companies' foreign borrowings, abandoned coordination of borrowings, and relaxed bank supervision.

In contrast to the Latin American debt crisis - interpreted as the result of wasteful/corrupt borrowing undertaken by governments as opposed to private firms operating in competitive markets - the AFC appeared to occur in opposite conditions. That is, most of the debt was private, and prior to the crisis, macroeconomic fundamentals - including growth, inflation and government budgets – all appeared fine (Wade & Veneroso, 1998:1).

Nevertheless the crisis highlighted the issues associated with rising asset values in countries which became unrealistically high as the money supply grew too quickly for the economy to absorb, thereby contributing to speculative booms in real estate and stock markets.

Indeed, Deputy Managing Director of the IMF Stanley Fischer (1998:9) drew attention to the role of 'lax prudential rules and financial oversight which had permitted the quality of banks' loan portfolios to deteriorate sharply'. This precipitated a reckless search for yield and fuelled asset price inflation creating a cycle whereby: risky lending drove up the risky asset prices, thereby making the financial position of intermediaries seem sounder than it was, which encouraged banks to engage in even further risky lending. As with any bubble though, the fall-out when it bursts had severe effects on the real economy. Crucially, when it did, it very quickly became apparent that those deficits which did exist were more problematic than initially assumed as they were funded largely by speculative short-term capital.

Drawing to varying degrees on these lessons the IMFs response to the crisis hinged on two main components - stabilization and adjustment - both broadly consistent with the response to the Latin American debt crisis. Firstly, in return for loans, countries deployed a set of macroeconomic policies deemed necessary to stabilize the economy. These consisted of targets for the permissible size of future budget deficits and tightening monetary policy.

On the one hand, fiscal contraction was deemed necessary to overall credibility and would both limit the need for overseas inflows of capital and ensure that government debt would not increase any more than was sustainable, with the alternative of printing money being 'potentially disastrous' (Fischer, 1998:12). In Thailand and Indonesia, fiscal contraction took the form of IMF advocated reduced budget deficits (cuts in social spending) so that money could be directed to restructuring banks, through postponing state infrastructure projects, and removing government subsidies and VAT exemptions (Karunatilleka, 1999:15).

On the other hand, of monetary policy, it was suggested that increasing interest rates would reduce the need for capital inflows and maintain export competitiveness by controlling domestic prices. Moreover, temporary rate increases were considered key to restoring confidence in the currency even if this complicated the situation of weak banks and corporations, because once regained, rates could return to normal levels. Taken together these policies, tightened monetary and fiscal policy were 'as it should be' (Fischer, 1998:11).

Secondly, accompanying rescue packages and macroeconomic prescriptions, the IMF also sought to implement adjustment policies to correct for perceived structural weaknesses in financial systems in affected economies, the aim being to remove 'impediments to growth' including monopolies, trade barriers and non-transparent corporate practices.

While adjusted for the needs of individual countries IMF programmes included: closing down or recapitalising troubled financial institutions; letting foreign financial institutions buy up domestic ones; requiring banks to follow Western prudential standards; requiring international accounting standards be followed and international accounting firms to be used for auditing purposes; to eliminate government directed lending; and to give up measures to assist individual firms avoid bankruptcy (Wade & Veneroso, 1998:5).

Here Krueger et al (2000:311) noted that if weaknesses in the banking system arose because banks took on too much risk yet states took only basic short–term measures to restore it to health and did nothing else, it would be failing in its duty to prevent a recurrence. Just as in the Latin American debt crisis, so again was the notion of un-sustainability drawn upon to provide the justification for stringent stabilization and adjustment policies. Although a range of factors were attributable to the crisis, the IMF firmly 'put the emphasis on shortcomings in domestic policies' (Moschella, 2010:102), particularly those relating to the banking sector.

Yet again however the IMF was criticised for attaching misguided conditions to programmes two of which were especially controversial. On the one hand, macroeconomic policies were manifest in: government spending cuts through austerity which called for small surpluses over programme periods despite economic contraction; and higher interest rates which further damaged a weak banking sector, worsening and prolonging the crisis.

On the other hand, IMF programmes required adjustment in areas that went far beyond addressing financial sector deficiencies. These distracted from issues of immediate concern, thereby creating unnecessary political opposition and damaging investor confidence by signalling that the crisis was worse than it was (Tagaki, 2009:118). Indeed, loan agreements incorporated a range of conditions and reform benchmarks than required previously despite observers diagnosing the crisis as one of premature financial liberalisation (Bhagwati, 1998; Stiglitz, 2002), rather than stemming from major structural problems.

Again, as with the Latin American debt crisis, the economic position of countries receiving IMF loans worsened enormously. On the one hand, GDP declined 13 percent in Indonesia, 10.2 percent in Thailand, 7.4 percent in Malaysia and 6.7 percent in the Republic of Korea in 1998 compared with the previous year. Moreover, from being stable prior, deficits were running negative at 1.7 percent for Indonesia, 2.8 percent in Thailand, 1.8 percent in Malaysia, and 4.2 percent in the Republic of Korea (ESCAP, 2002:39) a key reason being that expenditure was directed to debt servicing and restructuring financial institutions.

Although to varying degrees growth returned in the year or two following the outbreak of the crisis, its negative consequences persisted long after the initial shock. As with the debt crisis, the labour market that was particularly hard hit. In an Asian Development Bank Briefing Note assessing the social impact of the crisis Pernia and Knowles (2003:3) noted that unemployment rose by between 90 and 400 percent in affected countries between 1996 and 1998 which contributed enormously to increased instances of poverty.

Problems in the labour market however were not simply limited to those losing their jobs, but had important consequences for those that remained employed. On the one hand, in light of the crisis, firms cut wages and reduced employment benefits. Moreover, Pernia and Knowles (2003:4-6) observed that many people were now involuntarily working less hours and many older workers were being encouraged to take early retirement.

On the other hand under-employment increased substantially, with a common theme among crisis-hit countries being that the share of jobs in the lower paid agricultural sector increased as many were lost in the manufacturing and services sectors. This put further downward pressure on wages which were already low compared with other sectors (ESCAP, 2003:39). Taken together therefore, just as it had done in light of the Latin American debt crisis, 'critiques of the IMF's international crisis management role were given renewed political momentum and greater urgency' (Broome, 2010:43) due to its handling of the AFC.

Understanding neoliberal policy continuity

The two crises discussed here (among others) seemingly destabilised many of the cognitive assumptions, and had normative implications, for the neoliberal economic ideas under-pinning IMF policy priorities. Firstly, 'excessive exposure to external capital flows and the fact that in large part they were not oriented to productive uses were major factors in the build-up of economic crises in developing and emerging economies... beginning with the Latin American debt crises in the 1980s' (UN Trade and Development Report, 2014:122).

Indeed, the Latin American debt crisis and AFC demonstrated perfectly the inherent pro-cyclicality of capital flows, that is, how they flow out of a country during a recession precisely when it needs it most, yet flow in during a boom, thereby exacerbating inflationary pressures. This made developing countries subject to the rational and irrational whims of the investor community, to their irrational exuberance and pessimism, a scenario explained by Keynes who spoke of the "animal spirits" of the investor community (Stiglitz, 2020:100).

Secondly, the policy space to respond to crises was shown to be limited as governments resorted to external borrowing and felt compelled to bail out private debtors and socialise the losses associated with doing so. As a result, fiscal retrenchment exacerbated broader economic problems once manifest and had severe consequences for those groups least able to shoulder the burden of adjustment. Nevertheless, fiscal austerity, privatization and market liberalization were consistently advocated as ends in themselves, regardless of their consequences, as opposed to being the means to a more equitable and sustainable growth.

These conclusions precipitated a broader debate over how the IMF's international crisis management role, and the neoliberal international financial architecture centred on the belief in the efficacy of the market it sought to promote, should be reformed (Broome, 2010:44; Broome et al, 2012). At the very least the crises showed that the policies most conducive to growth were not universally applicable but dependent on an array of variables including a country's culture and stage of development. Indeed, Stiglitz (2004:3) noted that IMF statements to the contrary, there is no logical reason to believe that markets left alone will be efficient as no country has developed by simply opening itself up to investment.

This was a point not entirely missing on IMF staff members. Kreuger (2004:1) for example suggested that various crises, culminating in the AFC, 'forced some pretty radical rethinking' about the best ways to prevent and resolve them. This was manifest in the creation of the G20 in 1999, an annual meeting of finance ministers and central bank governors, which sought 'to provide a new mechanism for informal dialogue in the framework of the Bretton Woods institutional system, to broaden the discussions on key economic and financial policy issues among systemically significant economies' (G20, 1999:1).

This notwithstanding, no attempt was made to re-think the merits, or otherwise, of the neoliberal economic philosophy, nor was there any substantive effort made to reconsider the way in which economic problems were interpreted and responded to, and therefore, no shift in the kinds of policies pursued. Rather, Camdessus (1998:1) suggested that there would in fact be 'no new machinery, no more government intervention'.

Indeed, policy failures were explained away by the IMF by placing the blame at the feet of policymakers in developing economies, arguing that the underlying economic ideas were correct, but were imperfectly implemented due to technical governance failures (Killick et al, 1998). The IMF did not therefore abandon its core assumptions, despite the myriad pathologies presented by crises, but instead turned its attention to the implementation and monitoring of a greater range of neoliberal policies that would prevent or mitigate the worst effects of crises, and leave governments better placed to deal with their fiscal implications. Although the fact that it did appears puzzling, two reasons as to why are offered hereon in.

Understanding the nature of the IMF's response to financial crises

In order to understand why, despite the differences between the two crises discussed here they were interpreted and responded to in a broadly similar fashion, it is necessary to revisit the neoliberal economic ideas underpinning IMF problem definitions and policy priorities. Earlier in this chapter a number of developments in economics were highlighted that came to guide IMF actions including the rational expectations hypothesis, and it is adherence to this hypothesis, it is suggested here, that is implicit in IMF responses to the crises discussed.

Rational expectations assume rational actors maximising their utility in complete markets. In doing so, an assumption is made that, in forming their expectations, actors make efficient use of the information available to them, although the potential for random shocks is not precluded as they are not part of actors' information. Consequently, the efficient use of information provides actors with sufficient predictability to make expectations converge on average. This assumes that absent major informational asymmetries, actors' expectations about the future state of the economy should converge to promote a stable equilibrium.

What therefore, does this tell us about the nature of, and responses to, the crises discussed above? Given the foregoing it might be expected that holding the neoliberal economic ideas the IMF does, the crises would have come as a surprise. However, although the exact timing may have, those buying into rational expectations premises, including the IMF, accept their presence. Given this assertion, the IMF (1999:2) derived two key lessons from the crises. The first highlighted the need to increase information available to market actors, and the second, the importance of sound macro-economic fundamentals including low debt levels.

Learning the lessons of crises I: Increasing the provision of information

Should we accept the assumption of the presence of rational actors and therefore that the theory of markets corresponds to the actual condition of markets, it is entirely unsurprising that the key function of states is understood as being to provide actors with an information rich environment. After all, should equilibrium be built into the system then, it would be natural to assume that disequilibrium is primarily, albeit not necessary exclusively, down to informational imperfections. With the problem defined in narrowly circumscribed, functionalist terms as a lack of information, the solution was obvious 'more information, better information, more transparent institutions' (Best, 2003:375; Blyth, 2002a:11).

This approach was exemplified in light of the AFC by the G7 (1998:1) which observed that 'weaknesses in the financial sectors in some Asian countries increased their vulnerability to external shocks', yet 'had information about these developments been more widely available earlier, the international markets and International Financial Institutions might have been better placed to assess the risks'. The G7 was therefore clear about what it saw as the principal causes of the crisis, weak financial systems and a lack of transparency. As a result, solutions centred upon the need for better information, disclosure and transparency.

Similar conclusions were drawn by the IMF which pointed towards 'a lack of information as a central cause' (Best, 2010:32) which would therefore be crucial in preventing the effects of those in the future. Stanley Fischer (1998:15) for example noted that 'we have to do everything we can to provide the information and incentives that will encourage rational investor behaviour'. In a similar vein Managing Director Michel Camdessus (1999) suggested that 'a lack of transparency has been found at the origin of each recurring crisis in emerging markets', and they would continue to be inefficient, and would remain vulnerable 'in the absence of adequate, reliable, and timely information from all quarters'. As a result, the central IMF response placed considerable emphasis on the importance of information, along with great faith in the ability of markets to use it effectively.

By adopting this approach the G7 and IMF make the implicit assumption that the reason liberalized financial markets have proven inefficient, turbulent, and precipitating causes of the two crises discussed here is not inherent to their very nature. Rather, the crisis response suggests that financial markets can be subject to exogenous shocks whose worst effects can be mitigated through the increased provision of information which would allow for the adequate capture and calculation of risks, thereby leaving markets better placed to respond to signals and underlying economic fundamentals.

Learning the lessons of the crisis II: Macro-economic stability

The need to increase the provision of information so that rational actors would be better placed to respond to signals and mitigate the worst effects of crises, was only one of the key lessons learned from the crises. Indeed, this was considered a part of a broader strategy incorporating the second lessons, the need for a stable macroeconomic framework.

As a result the IMF has, if anything continued to broaden the scope of its policy concerns to include supplementary elements deemed key in contributing to stability and growth. This is demonstrable in its pressing - when a country's economic problems are considered deep seated - for the imposition of sound domestic financial systems, improvements in the quality of expenditure, increased transparency and accountability in government affairs to avoid policy mistakes that might waste national resources, and for deregulation and de-monopolization to create a level playing field for private sector activity (Fischer, 1998:6-8).

In particular however, Kreuger (2004:2) has stressed the importance of a country being suitably positioned to meet its debt servicing obligations during a crisis. Key here was an assumption that it was better for governments to enter a crisis with low levels of sovereign debt so that increasing fiscal demands would not excessively increase debt-to-GDP as this had the potential to increase interest rates on sovereign debts to un-sustainable levels.

This lesson was derived from the crises discussed here which Krueger et al (2003:316) suggested demonstrate how increase in domestic interest rates 'increases the prospective fiscal deficit because interest-carrying costs of the debt increase'. This is exacerbated by slowing economic activity, tax collections falling below prior estimates and increased fiscal expenditures. This therefore reinforced, in the eyes of those in the IMF, the need to provide a stable macro-economy and particularly, the need to control government finances.

Indeed, the need for increased fiscal responsibility has been an increasingly important element in arguments for a confidence-building strategy 'on the grounds that market operators and rating agencies usually attach great importance to fiscal balances when they assess credit risk' (UN Trade and Development Report, 2014:126). This view has driven the assumption that integration into global capital markets has a positive impact on fiscal discipline, and by implication, on macro-economic stability.

Implications for IMF understanding of crises: the role of FSAPs

The manner in which these respective crises were interpreted by the IMF implied that it was emerging economies' domestic problems in financial systems and 'lack of fit with the global financial system rather than the system itself' (Best, 2010:30) that was the key problem. By implication, what were needed were clearer, more universal rules to ensure global financial stability. This diagnosis not only implied a rejection of the need for a shift away from neoliberal economic ideas and policies, but in fact suggested the need for domestic political and economic institutional reforms in order to bring emerging market economies in line with the standards that existed in the most advanced countries where the prospects for financial and economic crises on a similar scale were considered negligible.

Of particular note in this regard was the establishment of the Financial Sector Assessment Programmes (FSAPs) introduced in 1999 in the aftermath of the AFC. These were aimed at addressing structural weaknesses in emerging economies, and providing better information to market participants. This represented an important change in the strategies deployed by the IMF in their efforts to better govern finance and development in both the national and international contexts as although the over-arching objective of helping to stabilize the international financial system was not new, the scope of the objective was novel.

FSAPs, by relying 'less on explicit coercion and more on the construction of new norms to achieve their ends' suggests that IMF actions can be best interpreted as part of a broader 'constructivist strategy' (Best, 2005:194-195). Understanding the production of FSAPs in such a manner allows us to foreground the politics, and thereby agency, associated with the production of reforms which can be viewed 'not simply as a technical process but also as a political and normative strategy designed to establish legitimacy for a particular form of international financial governance' (Best, 2005:200). This process was not regulative in the sense of seeking to regulate an extant activity, but was inherently constitutive in its attempt to re-shape the terms through which market participants interpret state actions. As a part of this process the IMF therefore proposed a new approach, one that would stabilise financial liberalization by imposing new domestic norms and institutions, effectively embedding finance from the top-down (Best, 2003:373).

FSAPs are premised on the assumptions that financial sector development is an important means to spur economic growth, and that well-regulated financial systems are essential for macro-economic and financial stability in a world of increased capital flows. The aim of FSAPs is therefore to develop a set of international standards that the IMF believes all states should adopt, and to support member countries' efforts to strengthen their financial system by 'facilitating early detection of financial sector vulnerabilities, identification of key development needs, and to prioritize policy responses and provide technical assistance when needed to strengthen supervisory and reporting frameworks' (Krueger, 1999a:6).

Key in this regard was an attempt by the IMF to increase the flow of timely and accurate data by encouraging countries to move towards greater transparency and disclosure; and acknowledge that it will be necessary to strengthen the standard of this information, for example, by providing data on forward transactions by central banks. Doing so, it is believed, leads to better informed investor decisions and better policies by governments.

The consequences for domestic financial systems were apparent. Here, the IMF was important in helping to coordinate and communicate, along with the World Bank, BIS, and international standard-setting bodies, a set of standards and best practices in the banking area that have worked well in other countries and could be adapted and applied in others.

As a result, effective surveillance of national financial systems, 'along with a harmonization and international convergence of key components of financial policies' it was suggested, will help minimise risks and promote development of the financial system (FSAP Handbook, 2005:1). This constituted an attempt to make the financial systems of developing countries closer resemble those of the West who were thought better placed to respond to the risks of increased financialization, and therefore served as a model for financial practice.

In addition to the need to implement a range of financial sector policies however, it was also observed that there are important and 'close two-way linkages between financial sector soundness and performance, on the one hand, and macroeconomic and real sector developments, on the other hand' (FSAP Handbook, 2005:1). As a result, adhering to the importance of both was considered necessary for overall financial and economic stability.

On the one hand Kose et al (2007:7) have suggested that financial sector liberalization and deregulation by increasing the potential costs associated with weak domestic policies, and by implication enhancing the benefits of the pursuit of good ones, would help to impose discipline on macroeconomic policies. That is, because 'liberalization makes a country more vulnerable to sudden shifts in global investor sentiment, it can signal a country's commitment to better *macroeconomic* policies as a way of mitigating the likelihood of such shifts and their adverse effects'. In particular it is shown to produce better monetary policy.

Indeed, it was suggested that keeping a close eye on broader macroeconomic developments would play an important part in drawing attention to the potential for future financial crises. This would include, analysing macroeconomic forecasts, financial sector indicators, along with tax policies, which 'would help to form a view on the likelihood of shocks to the financial system from the broader economic environment' (FSAP Handbook, 2005:7).

Assuming particular importance however, and playing 'a major part of the Fund's role', was 'working with members to reduce fiscal deficits' both during good times and crises, so that governments were better placed to absorb their impact, a process described as 'difficult, but essential' (Krueger, 2003:5). This was to be achieved through more efficient tax structures with fewer exemptions and a broader base but at lower rates, and effective budgeting and expenditure controls which were considered particularly essential.

Taken together therefore, the IMF retained its primary focus on inflation targeting, sound money, prudent fiscal policies, open markets and respect for property rights and good governance as preconditions for macroeconomic stability and growth, a commitment which continues to constitute the core of Fund supported programmes.

The IMF is almost exclusively concerned with the provision of cognitive justification for policies consistent with the neoliberal economic philosophy and problem definitions, and FSAPs, presented as a neutral, technical enterprise with emphasis on better data collection and transparent institutions were largely couched in such a manner.

Moreover however, in this instance, the act of persuading states of the necessity of such reforms, Best (2003:75) suggests that 'if we attend to the language of its advocates, it becomes clear that this new governance strategy is actually self-reflexively normative'. That is, the IMF has also framed the need for reforms in 'powerfully normative terms as part of a new "global ethics" in which states take responsibility for their contribution to global financial stability' (Best, 2005:195) through the adoption of sound economic policies. This was typified by successive Managing Directors within the IMF who have spoken in explicitly normative terms of the need for "solidarity and responsibility" (Camdessus, 1997), "global ethics" (Kohler, 2002) and a need to do what is "morally right" (de Rato, 2004).

The up-shot of doing so demonstrate that the approach taken by the IMF 'was not purely technical and value-neutral; they aimed to reconstitute these economies to conform with the market-dominated models' (Barnett & Finnemore, 2004:47). In doing so, what FSAPs leave states with is in fact a narrowly constituted system, with an intellectual and technical language which specifies approved categories and terms which form the basis of discussion.

Using these however restricts what is thought by specifying the parameter of what was is acceptable in the financial sector liberalization debate. This intellectual language ensures that politicians and policy-makers are talking about the same thing by defining only a limited space of communication. As a result, what actors are left with is a series of Anglo-American laissez-faire prescriptions for sound economic practices rather than a broadened scope for alternatives better oriented towards domestic contingencies that might actually be better placed to achieve their aims.

In doing so, the IMF 'clearly excluded several alternative economic strategies from the outset' (Best, 2005:196) and in doing so has sought to internationalize and institutionalize not only a particular set of practices, but also a specific vision of what an appropriate economic order should look like. As a result, the new standards can be shown to have had as much to do with power and normative assumptions about what is right as it is to reduce uncertainty. However, power in this instance is not simply the power to exert ones will over others, but lay in the constructivist aspect of the initiative that it seeks to instantiate, that is, the constitutive nature of a particular set of rules and practices. Crucially, this constructivist strategy is not simply an attempt to alter behaviour, 'but more profoundly to redefine what it means... to be good economic *subjects* both domestically and globally' (Best, 2005:196).

In seeking to foster a broad convergence of economic governance practices, the IMF therefore sought to play a much greater role in shaping domestic policies than it has so previously. Most of these are however, based on industrialised countries current practices and therefore designed with no substantive input from developing economies.

Viewed in this regard, new standards do more than simply create clarity for existing agents inasmuch as they 'are intended to constitute new state interests and identities, to create a particular kind of "normal state" that is defined in large measure by its support for a particular kind of free-market economy' (Best, 2005:202). Consequently, while the ultimate goal of contributing to domestic growth along with international financial stability, the aim was to do so in very narrowly circumscribed terms and at a very significant cost to particular states (those can least afford to partake in such an undertaking).

Conclusion

This chapter has served two purposes. On the one hand it has drawn attention to the initial remit of the IMF which was premised on a particular interpretation of the causes of the negative consequences associated with the inter-war years and what this meant for policy-makers. At this juncture problem definitions and policy priorities were provided for by the Keynesian economic philosophy which stressed an important role for the state in managing the economy. Thereafter, it was shown how the inflationary and growth crisis, interpreted as a crisis *of* Keynesianism, ultimately presaged a shift to neoliberal economic ideas which have informed IMF problem definitions and policy priorities in crisis contexts since.

On the other hand, it was demonstrated how the IMF has altered the manner in which it has responded to financial crises, that is, through greater involvement in not only stabilizing crisis-hit countries, but by seeking the implementation of a range of adjustment policies, both of which were more closely associated with adjustment under the gold standard as opposed to the BWS. The record in doing so however was shown to be dire. Nevertheless, the IMF did not deviate from the prevailing set of neoliberal economic ideas, but instead called for greater information, transparency and disclosure so that markets would be better placed to react to signals to prevent the worst effects of crises, a key assumption of which was that, had the financial sectors of crisis-hit countries more closely resembled those of the West, they would have either been prevented, or better mitigated.

The preceding discussion notwithstanding, the following chapter addresses the nature and causes of the current downturn. In doing so, it is demonstrated how although variously conceptualised initially, two failures, financial sector liberalization and deregulation, and monetary policy, suggested the potential for a crisis *of* as opposed to *for*, neo-liberal economic ideas.

Chapter 3

Contextualising the failure of neoliberal economic ideas

'Markets do not always know better than governments; private greed does not procure public benefits; hedge funds and investment banks are not wealth creators, they are wealth destroyers; a rising tide does not invariably float all boats'
(Marquand, 2011)

Introduction

In 2008 advanced economies were faced with what has been contextualised as 'the greatest crisis in the history of financial capitalism' (Turner, 2009:2), characterised by contracting global growth, recessions in developed economies, and the deployment of substantial fiscal stimulus to shore up ailing economies. Against this backdrop, this chapter demonstrates how, on the one hand the downturn was initially interpreted as being the result of inadequate policies deployed in an otherwise relatively stable economic framework.

On the other hand, it is demonstrated how, as the downturn intensified, there developed a broad consensus that the failure of neoliberal economic ideas were in fact a major precipitating cause of the increasingly dire economic environment facing policymakers. This is explored with reference to two key failings, financial sector liberalization and deregulation which was the crucial precipitating cause of the downturn, and of monetary policy to prevent the transmission of the financial sector failings to the real economy.

Finally, it is suggested that although the failure of neoliberal economic ideas provided the pre-conditions for a crisis narrative, change has not been forthcoming. In helping to understand why, it is suggested that the financial and economic downturn progressed along three phases, each requiring a distinct response and each having differing implications for the neoliberal economic philosophy, problem definitions, and policy priorities, the implications of which are explored in chapter's four to seven. The first phase was limited to the banking and financial sectors; the second phase occurred as banking and financial sector pathologies spilled over into the real economy; and the third phase occurred as fiscal stimulus undertaken during the second phase led to soaring sovereign debt burdens.

Contextualising the downturn

In the latter half of 2008 the Western banking system faced collapse. What began as a disturbance in a relatively small segment of American finance, the subprime mortgage market, cascaded quickly beyond both the housing market and US borders, disrupting much of the world's financial system and casting a pall over economic growth prospects.

In the US, mortgage companies Fannie Mae and Freddie Mac were placed under the conservatorship of the US Federal Housing Finance Agency with the pledge of government finance as needed, Lehman Brothers collapsed into bankruptcy, and Merrill Lynch was sold to Bank of America. Similarly, UK banks were nationalized or part nationalized, mergers and acquisitions were facilitated by the government, and banks received significant state financed cash injections. This was, to varying degrees, a scenario replicated the world over.

Banking and financial sector pathologies quickly spilled over to the real economy, causing world economic activity to contract in 2009 for the first time since the end of World War Two. The US for example, the world's foremost economic power, witnessed a dual crisis of doubling unemployment and contracting gross domestic product (GDP) (Jones, 2009:2). Likewise, in the UK, annual GDP declined in both 2008 and 2009 (World Bank, 2014) as a result of its enormous housing bubble and reliance on financial sector growth. In the Eurozone, overall GDP declined in both 2009 and 2012 (Eurostat, 2014), with Portugal, Italy, Ireland, Greece and Spain proving particularly vulnerable to the economic downturn.

In addition to the Northern core, many of the world's peripheral economies were adversely affected. In sub-Saharan Africa per capita GDP declined from 3.1 percent in 2008 to -0.6 percent in 2009 (IMF, 2009:2) with the poorest countries within the region being especially hard hit due to the decreasing demand for exports and collapse of commodity prices on which the least developed countries relied on most heavily.

Although Chapter 2 observed the increasing prevalence of financial and economic crises in the contemporary era, they have tended to remain limited to what Broome et al (2012:10) have referred to as 'an "other" geographical realm', and have as a result, remained limited, relatively speaking, in their scope or relevance. The current downturn can therefore be considered unique inasmuch as although its origins were the industrialised countries, the negative effects thenceforth permeated economies the world over.

In tracing how the downturn came about, a typical narrative proceeds along the lines that in the 1990s, developing countries borrowed to finance investment. However, financial crises such as those in Asia (1997), and Russia (1998) created a situation in which developing countries sought to shore up their balance sheets by saving more and borrowing less. This, coupled with a number of oil producing countries carrying large surpluses due to increasing commodity prices, created a situation in which developing countries went from *borrowing* \$88 billion in 1996 to *lending* \$205 billion by 2003 (Jones, 2009:3). Capital markets, suddenly awash with cash, and with interest rates low, sought increasingly profitable investment opportunities, and it was in stocks and shares, and property that investors sought solace.

As property prices continued to rise, this was coupled with an increasing utilisation of mortgage backed securities, the so-called 'greatest financial innovation of the 20th Century' (Shah, 2009:4), which although present for a number of years, became the financial instrument of choice in light of the dot.com bust (Sinclair, 2009:451). Banks were able to slice and dice their loans into saleable assets and thus sell them, and any associated risk on. In doing so, it was argued that securitisation would make the banking and overall financial system more resilient (Turner, 2009:42). However with the prime mortgage market heading toward saturation and with interest rates at historically low levels, investors were prompted to search for yield further down the credit quality curve (Anderson, 2009:2). Consequently, by 2006 one fifth of US mortgages were sub-prime yet this was deemed unproblematic as property prices continued upon a seemingly relentless upward trajectory (Jones, 2009:6).

It seemed to be a foolproof plan and, somewhat unsurprisingly, investors sought a greater piece of the pie. Traditional high street banks therefore entered into investment banking, transferring their business models in order to compete with the less regulated institutions of the shadow banking system which, in turn, got into high street banking to such an extent that it grew as large as the formal banking system albeit bereft of comparable regulatory structures. Such was their apparent success however that anyone questioning the logic of this approach was deemed to be anti-capitalist or simply socialist (Shah, 2009:25).

By 2006 however, with the tendency towards low interest rates reversing, 16 percent of sub-prime lenders on variable rate mortgages in the US entered into default (Jones, 2009:6). Initially, it was unclear to what extent banks had been affected by the collapse in the sub-prime market or the extent to which other banks were backed by bad, or so called 'toxic' debt. Bereft of credible information and with banks cautious of lending to one another, the inter-bank interest rate on short term loans increased from 0.2 - 0.4 percent prior to the downturn up to 3.5 percent in 2008 (Jones, 2009:7). Lending was therefore either at a premium or non-existent, thus signalling a classic liquidity crisis.

At this juncture, it was apparent that the market was ill-equipped to handle the crisis without disastrous consequences, not just for the financial sector, but the economy in general. Indeed, having seemingly falsified the belief that market discipline and self-regulation would provide an excessive brake on risk-taking by unregulated institutions, banking and financial sector pathologies contrastingly illustrated the inadequacy of market discipline. As a result, as economies faltered, governments were faced with no viable alternative other than to assist banks financially or facilitate mergers and acquisitions in addition to injecting significant fiscal stimulus in an attempt to redress the ensuing economic downturn.

Conceptualising the downturn

This generally accepted narrative of the origins of the downturn notwithstanding, there nevertheless existed an initial lack of consensus on how best to conceptualise its nature, thereby leading to myriad technical explanations. For Carmassi et al (2009) the result was lax monetary policy (supplemented by excessive leverage and reckless bets on asset price increases), without which the unfolding turmoil would not have been possible. In making this assertion, the authors singled out the role played by the Federal Reserve in repeatedly intervening to counter negative bubbles over the course of a decade by aggressively cutting interest rates. Such an asymmetric monetary policy however, both played an important role in bringing about convergent expectations of ever-rising asset prices, and created a gigantic moral hazard problem in which all agents expected to be rescued from their mistakes.

Former Federal Reserve Chairman Alan Greenspan (2008:507) however suggested that 'the fundamental problem had been the under-pricing of risk worldwide'. Here, Greenspan noted that in June 2007 the yields of CCC-rated junk bonds in the United States had shrunk to little more than 4 percent over yields on ten-year US treasuries which were vastly safer. By contrast, in October 2002, the yields of the two were more appropriately risk weighted and separated by 23 percent (Greenspan, 2008:507-508).

This mispricing of risk was, according to Greenspan (2008:510-513), driven in large part by developing country growth, particularly in China whose citizens chronically save more of their incomes than do those in developed nations. The resulting rise in what economists call saving propensity swamped the financial markets as planned capital investments did not keep pace with savings. As a result, long-term interest rates, both nominal and real, fell dramatically around the world, as did inflation, and drove the prices of assets up sharply.

As a result, investment banks and private equity funds were all awash with cash thanks to massive increases in liquidity. It was against this backdrop that investors reached out to acquire lesser-grade assets in order to enhance returns that had been squeezed by the decline in long-term rates. Yet it was the failure to properly price such risk that typified the downturn as when markets eventually trashed the rosy ratings, a blanket of uncertainty descended on the investment community with banks hiking inter-bank lending rates. As a result, when the downturn hit, its suddenness was a shock, but the fact of it was not.

Friedman and Friedman (2008) however suggested that the financial collapse demonstrated what can go wrong when firms do not behave ethically or socially responsible. At base, the authors noted that the context within which this kind of corporate behaviour flourished was derived from a widespread, yet misplaced interpretation of the work of Adam Smith, which appeared to suggest that self-interest and the invisible hand of the market-place constituted the most efficacious means to allocate scarce resources. This resulted, in a system that for corporations was synonymous with the maximization of profits and/or shareholder wealth.

However, raw self-interest without a foundation of morality was not what Adam Smith was about. Indeed, the authors suggest that the financial meltdown showed quite clearly what happens when everyone is solely concerned with their own self-interest. This, the authors suggest, was the most important lesson of the downturn: unethical behaviour has severe adverse economic/political consequences. An assumption was therefore made that the financial collapse could not have occurred if all parties were socially responsible, were not motivated by greed, and were compensated/incentivised in the perverse manner they were.

These conceptualisations draw our attention to the fact that a given set of economic and political pathologies can support a multitude of differing and competing interpretations and narratives of what went wrong, which actors and policies were at fault, and crucially, what policies are required to place the system back on a sound footing (Hay, 1999, 2013a). In this particular instance however, those above all foresaw the need for intervention to redress existing policies that were generally of the correct order but would need some tinkering so as to guarantee the continued functioning of an otherwise stable financial/economic order.

Carmassi et al (2009) for example suggested that all that was required to avoid a repeat was to correct the policy faults of lax monetary policy, and to a lesser extent, excessive leverage. An assumption was therefore made that there was no need for intrusive rules constraining non-bank intermediaries and financial innovation. Rather, the message remained, keep things simple. Similarly, Friedman and Friedman (2008:4) suggest that one of the key lessons from of the downturn is that ‘we should recognise that what we have experienced is not the breakdown of an economic system. This is a values meltdown more than anything else’.

Although these conceptualisations represent useful explanatory tools of the origins of the present downturn, they nevertheless belie a more pressing need to identify the more fundamental, underlying problems that created the current situation (Boone et al, 2009:8).

In seeking to provide a deeper understanding of its origins, an assumption is made, in a manner consistent with Krugman (2009) for example that the shift from the Keynesian to neoliberal economic ideas was the critical precipitating factor. Against this backdrop, the financial, and latterly economic, downturn can be shown to rest on the culmination of two key failings central to neoliberal economic ideas. The first of these was the failure of banking and financial sector deregulation and liberalization. The second was the failure of monetary policy to prevent its transmission to the real economy and a broader economic downturn.

This had profound implications for the economic ideas underpinning the neoliberal economic philosophy (assumptions regarding the efficacy of the market), the manner in which economic problems are interpreted and responded to (an emphasis on monetary policy as a means by which to control inflation and mitigate the most severe effects of economic downturns), and the kinds of policies pursued (financial sector liberalization).

Drawing attention to the failure of neoliberal economic ideas as a precipitating cause of banking and financial sector pathologies, and the broader economic downturn, carries with it an important implication: that what we are seeing is not simply the result of an exogenous shock punctuating an otherwise stable economic order, or following Sinclair (2009:451), 'a deviation from the normal state of the market'. Rather, it is understood for our purposes here, consistent with Hay (2013:4) as, more fundamentally endogenous, arising from the internal puncturing of the neoliberal model of growth. It is therefore not possible to place responsibility onto emerging markets whose financial sectors were not aligned with those of the West as this was a problem created by the very financial sectors of those considered best place to avoid such shocks in the first place. Indeed, responsibility for this downturn can be placed squarely at the feet of the neoliberal economic ideas and practices advocated by global governance institutions, including most notably, the IMF (Best, 2010:31).

Failure I: Financial sector liberalization and deregulation

In understanding the first of the failures it is useful to draw on the work of Crotty (2008:3) who has noted that the deeper cause of the current turmoil 'is to be found in the flawed institutions and practices of what is often referred to as the New Financial Architecture (NFA)' or for the purposes of this research, financial sector liberalization and deregulation associated with neoliberal economic ideas. That is, the integration of modern day financial firms and markets with an associated regime of light government regulation. Although having existed for twenty five years Crotty notes that a 'perfect calm' between 2003 and 2007 characterised by low interest rates, low loan default rates, high profits and rising stock prices, all contributed to the excesses that ultimately precipitated the financial collapse.

In particular, firstly, innovation created financial products that were so complex and opaque they could not be priced correctly and therefore lost liquidity when the perfect calm ended. Indeed, financial innovation reached such a point that structured financial products including mortgage-backed securities (MBSs) and collateralised debt obligations (CDOs) were so complex that they 'destroyed the transparency necessary for any semblance of market efficiency' (Crotty, 2008:25), being as they were, characterised by asymmetric information and unequal bargaining power that allowed banks to generate high profits.

In reality, dealers in structured financial products deliberately ensured that clients did not know the true price of what was being traded, rather, a lack of transparency was at the very heart of the profitability of structured products as clients were denied access to up to date prices due to complex pricing structures. This blew out of the water the claim that financial markets, left alone, would provide enough information for risk to be optimally priced.

Moreover, the crucial foundation of the narrative claim that commercial banks would distribute almost all risky assets associated with innovative financial products to capital markets and hedge whatever risk remained through credit default swaps turned out to be completely false. On the one hand, rather than shrinking as the narrative predicted, on-balance-sheet assets of large global banks increased from $10 trillion to $23 trillion between 2000 and 2006 (Crotty, 2008:31), the cause of which was increased bank holdings of MBSs and CDOs, the exact securities that the narrative claim suggested would be sold to markets.

CDOs were especially attractive since they could be held off-balance-sheet with no capital reserve requirements. These were kept for four main reasons. First, to convince potential investors of their safety; second, substantial shares of the riskiest products were kept to maximise compensation by maximising short-term profits; thirdly, the time lapse between bank's receipt of a mortgage and the sale of the MBS/CDO was sufficiently long that at any point in time banks held or warehoused substantial quantities of these securities; fourthly, when banks found the safest or 'super senior' tranches of mortgage backed securities hard to sell because their yield was low, they simply kept them themselves (Crotty, 2008:32-33).

On the other hand, under the prevailing regime, regulators allowed giant banks to measure and manage their own risk and set their own capital requirements which, given perverse incentives, naturally led to excessive risk-taking. Indeed, in 1996 the BIS sanctioned the idea that as of 1998 regulators should shift responsibility for setting limits on giant banks' risk from regulatory authorities to the banks themselves. This edict was a core component of the Basel 2 regulatory regime in which banks would manage risk through a statistical exercise known as Value at Risk (VAR), allowing banks to set their own capital requirements.

VAR is an estimate of the highest possible loss in the value of a portfolio of financial assets and liabilities over a fixed time interval with a specific confidence level. However, there were three fundamental flaws in this model of risk assessment: firstly, there is no period of historical data that can generate a reliable result; secondly, VAR assumes that substantial 'shocks' to the financial system that occur every five or six years cannot possibly take place; finally, the assessment of asset price correlations based on historical data used in VAR calculations becomes grossly unrealistic when the system fails (Crotty, 2008:38).

Secondly, financial sector liberalization and deregulation was shown to encourage perverse incentives that create excessive risk, exacerbate booms, and generate severe downturns. This is especially so during financial upturns as risks build up, creating even higher leverage and financial stability. Indeed, Crotty (2008:19), following Keynes, suggests that the financial sector is one that is particularly susceptible to herd behaviour (see Chapter 2). This was perhaps best exemplified by Citigroup Chief Executive Chuck Prince's comment that 'as long as the music is playing, you've got to get up and dance' (quoted in Financial Times, 2007:1).

In this particular instance, the financial collapse demonstrated for example how contracts to manage large portfolios can be lost by a firm if its returns fall below the industry average. As a result, when the asset bubble took hold institutional investors had a strong incentive to follow others in pursuit of capital gains, even at the risk of absorbing losses when the bubble burst. Therefore, even managers convinced the bubble will deflate must follow the herd as not doing so would risk losing business. If they follow the herd and the bubble bursts however, all firms suffer losses and so none will lose their competitive advantage. This explains why such a range of institutions became major investors in securities markets.

Thirdly, the preceding discussion shows how such flaws have major implications for the theoretical foundations of neoliberalism. On the one hand the banking and financial collapse demonstrated the extreme gap between theoretical assumptions and real world markets, notably, that capital markets are efficient and price risk and return correctly; and liquidity is always perfect (assets can be sold any time at their equilibrium price) (Crotty, 2008:14).

Rodney Bruce Hall (2009:453) for example has observed, following Minsky, that contrary to the efficient markets hypothesis, 'market prices of financial assets do not reflect "correct" prices based on current information, but market actors acquire financial assets on the shared expectation that they will rise'. As a result, rather than calculating utilities in accordance with rational expectations actors instead operate on the basis of shared social and economic understandings that they derive from one another. This ultimately leads to periods of excessive credit creation in the economy and the mispricing of financial risk.

On the other hand, this has important implications for the manner in which actors are perceived to act on the basis of rational expectations. Indeed, unfolding financial sector pathologies demonstrated that actors act upon the basis of inter-subjective expectations. That is, they look to each other for signals as to how to react to market events. When these shared understandings are disappointed, they panic, thereby contributing to volatility. The current turmoil is therefore but one example in which the behaviour of market participants diverges from the behaviour predicted by rational expectations theory (Hall, 2009:454-455).

In doing so, it was demonstrated that: agents can not know the future because it does not yet exist, they have to make guesses based on some process of extrapolation based on the past; as a result, in a world of uncertainty, risk aversion is endogenous and varies with the cycle, that is, investors got both more optimistic and less risk averse during the boom years which caused leverage to rise as the boom accelerated; yet when the downturn broke out, pessimism set in and risk aversion and liquidity preferences spiked, thereby causing investors to sell risky assets. This destroyed liquidity in troubled markets to such an extent that assets could only be sold at a large capital loss (in 2007 for example Wachovia Corp. bought a CDO for $600,000 but within a few months was willing to accept just one twentieth of this initial price) which accelerated the rate of price decline (Crotty, 2008:30).

Taken together therefore, on a fundamental level, the banking and financial sector collapse problematised many cognitive assumptions underlying the neoliberal economic philosophy including: the "efficient market hypothesis"; the "rational expectations paradigm"; and the "self-regulation of markets and institutions". In this respect, it appeared evident that the collapse was not simply a failure *for* neoliberal global economic governance, but was a far more fundamental failure *of* neoliberal economic ideas, the manner in which economic problems are identified and interpreted, and the kinds of policies considered appropriate.

That is, the banking and financial collapse demonstrated that: markets do not know better than governments; private greed does not procure public benefits; investment banks and hedge funds are not wealth creators, they are wealth destroyers; a rising tide does not float all boats as wealth has not trickled down from the ultra rich to the rest; such a model is monstrously unjust and morally unsustainable; and the financial innovations of the past, premised on the notion that risk is knowable and calculable, does not constitute a scientific basis upon which to form a calculable probability (Marquand, 2011; Abdelal et al, 2010:233).

Failure II: Monetary policy

Although banking and financial sector regulatory failures were readily apparent, 'linking the explosive banking and financial crash of 2008 to macroeconomic policy and problems is a less straightforward intellectual case to make' (Baker, 2015:359), despite it being assigned ‘a central role’ (Bernanke, 2010:1) in the downturn. Indeed, that a number of failings have been attributed to it means that the nature of the lessons to be learned is controversial.

Firstly, it has been suggested that monetary policy failed to prevent the banking and financial collapse. This line of critique proceeds along the lines that monetary policy did not pay sufficient attention, and therefore did not seek to effectively counter, the unfolding house price bubble. Proponents of this view therefore limit their calls for an expanded mandate and a greater role for monetary policy in preventing and controlling bubbles.

Secondly, it has been suggested that monetary policy failed because rates were kept too low for too long a length of time. This, the argument proceeds, contributed to an abundance of cheap money which, particularly during the first half of the decade helped cause a house price bubble. Those highlighting these failings typically daw on the example of simple policy rules, namely the Taylor Rule which provides ‘the most commonly cited evidence that monetary policy was too easy during the period from 2002 to 2006’ (Bernanke, 2010:7).

These two approaches highlight how policies could have been deployed more effectively to prevent the economic downturn. Accordingly, an assumption is made that monetary policy could have been much more proactive. Nevertheless, the focus here is on a third failure, the actual functioning of monetary policy of the kind often advocated by the IMF to deal with developed country downturns. This typically takes the form of interest rate reductions as the signs of an economic slowdown present themselves, as was the case in initially dealing with the downturn as banking and financial sector pathologies affected the real economy.

However, in the case of the current downturn, interest rate reductions ran into trouble as rates quickly fell to, or very near to, the zero lower bound (ZLB), thereby limiting the role of monetary policy as the first line of defence. Moreover, increasingly unconventional monetary policies also failed in their ability to prevent the financial and economic downturn from becoming a far more serious collapse in economic demand. In helping to explain why this is so, it is useful to draw on research presented in the IMF's October 2008 GFSR.

It was a commonly assumption that, for developed countries at least, cutting the bank policy rate (typically an overnight rate) during times of economic slowdown/recession would be transmitted through interbank and money-market interest rates, so influencing consumer and business lending rates and by implication, domestic demand. However this transmission mechanism failed to operate in a manner consistent with conventional thinking during the current downturn thanks largely to the inter-connections between money and other credit markets that have developed over the past two decades. This shows how disruptions to money and funding markets can have important adverse macro-economic consequences.

Although structural changes in the financial sector of the last twenty five years or so did not appear to have undermined the traditional monetary policy transmission mechanism, these changes had in fact set the stage for the alteration in the transmission mechanism which were particularly evident beginning in summer 2007 (GFSR, 2008a:81). The most important of these changes has been the increasing prevalence of near-banks, the shift of banks towards market financing, and the shortening of long-term liabilities through the late-1990s.

In the first of these, near-bank financial institutions (including issuers of asset-backed securities and other structured products, finance companies, securities brokers and dealers, and funding corporations) have gained a significant share of financial intermediation, and now account for an increasing share of the financial sector, the corollary of which has been a corresponding declining share for banks, particularly throughout the 1980s and 1990s.

In the second of these, banks have been moving away from deposits to more unreliable market-based financing. In doing so, “core deposits” have been replaced by a range of other managed liabilities. This has links with an originate to distribute financial model that relies heavily on sound short-term market liquidity management. Similarly, the share of deposits held by households has declined over time, while simultaneously, deposits held by non-financial corporations and financial intermediaries have increased. Moreover, financing through repurchase agreements and issuance of debt securities have expanded, indicating that banks are increasingly exposed to developments in money markets (GFSR, 2008a:84).

Finally, bank liability maturities have shortened and become more volatile in the process. These short-term markets became more important for banks and near-banks through the 1990s as a more flexible way of managing their asset and liability structures. In doing so, banks have tapped an increased share of funding through repo agreements. The problem with doing so, however, is that short-term market financing costs are more volatile than the traditional main financing source of core deposits.

With the preceding discussion in mind, the GFSR (2008a:85) has suggested that ‘the dramatic alteration in the interest rate transmission mechanism brought on by the market turbulence that erupted in July 2007 can be seen in the changing costs and composition of bank and near-bank financing’. That is, interest rate spreads and the volatility of banks’ short-term financing rose to levels exceeding those of previous downturns, immediately raising marginal financing costs, and in so doing, cut off some banks from the markets.

Banks and near-banks were therefore left with no viable option other than to tap longer-term financing, despite the higher costs associated with doing so. The result however was that the spreads over treasury securities of comparable maturities of longer-term bank financing instruments shot up to levels far above previous cyclical highs such that banks significantly tightened lending standards for most categories of loans (GFSR, 2008a:86).

This evidence did not fundamentally challenge the assumption that the medium to longer-term pass-through of policy rate cuts was mostly stable over time, as a relatively smooth long-run transmission of policy rate changes to market interest rates testified. What it did do however was suggest short-term pass-through coefficients were inherently problematic.

Indeed, particularly from mid-2007 (about the time the turbulence began), three-month rates, most notably LIBOR (the London Inter-Bank Offered Rate) ‘jumped substantially at the same time as the extraordinary increase in money market spreads and the collapse of the structured credit market in response to subprime mortgage market distress', which, along with being even more pronounced for near-banks, pointed towards 'evidence of a dramatic alteration in the predictability of interest rate transmission' (GFSR, 2008a:91).

This suggested that the early linkages of interest rate transmission were impeded by the financial nature of the downturn which became disconnected from actual rates. This helps to explain why, despite the substantial decline in policy rates and interest rates on securities for example, the cost of credit to households and businesses rose, sometimes substantially.

Given the foregoing, 'the tightening of credit standards and the failure of the cost of credit to households and businesses to fall despite the sharp easing of monetary policy has led to a common view that monetary policy has not been effective during the recent financial crisis' (Mishkin, 2008:1). Indeed, contrary to existing assumptions regards the transmission effects of monetary policy interventions, the economy went into a tailspin. Therefore, its use was likened to pushing on a string. This led to two conclusions. Firstly, if monetary policy is in-effective, there was no reason to use it to cope with the downturn. And secondly, easing monetary policy during a financial collapse can be counter-productive because it can weaken the credibility of monetary authorities to keep inflation under control.

In light of the failures detailed here, the comment by Romer (2009:12) that 'the system that allowed our current crisis to occur cannot be permitted to continue' became commonplace, and was also supplemented with calls in some quarters for the need for a shift away from prevailing neoliberal economic ideas (Johnson, 2009:4). This reflected a widely held assumption of the time that the downturn 'was likely to induce profound changes in economic theory, philosophical outlook, and institutional structure' (Sheng, 2009:375).

Indeed, it was argued that 'at the very least the prospect of a substantial redrawing of the importance of finance and the scale of its activities... as well as much tighter regulation... were widely anticipated as the minimum changes that would be needed' (Gamble, 2009:70). Certainly, it was assumed that banking and financial sector pathologies, along with the protracted economic downturn had been at the very least as severe as other similar periods of political-economic failure (the Great Depression of the 1930s and stagflation of the 1970s) that presaged a crisis, and therefore major transformation of their respective orders.

IMF responses as a multiphase event

Having highlighted the failure of two areas synonymous with neoliberal economic ideas, the empirical chapters that follow provide an assessment of the extent to which these have impacted upon the neoliberal economic philosophy, problem definitions and policy priorities in the IMF. Before doing so however, three considerations are noteworthy.

Firstly, how the IMF interpreted unfolding events was hugely important as at its Sao Paulo Summit, the G20 noted that 'we must draw policy lessons from the current crisis... to minimise the risk of a future crisis', and that 'given its near universal membership and core macro-financial expertise, the Fund should play a leading role in this task' (G20, 2008:5). Moreover, the G20 group of state leaders increased the funds available to the IMF so that it would be ably positioned to respond to requests for assistance by countries. Taken together we can see how the IMF was accorded a key position in responding to unfolding events.

Secondly, differing diagnoses of the downturn implied the need for alternative policy interventions. Certainly, in not being given by their material conditions, the failure of neo-liberal economic ideas are differently experienced by agents, so what failure meant to some might not be as obvious to others, yet this discursive process is crucial as the diagnosis that sticks not only shapes the response, but shows what is (im)possible to others (Abdelal et al, 2010:233). The question therefore is how has the IMF interpreted such failures, how has it spoken of what they are, and what models has it suggested might legitimately be brought to bear in terms of response.

Thirdly, given the foregoing, understanding how the IMF has conceptualised the unfolding turmoil will play an important part in helping us to determine the extent to which neoliberal economic ideas continue to be perceived as the superior means by which to respond to the downturn. Namely, can the solutions to questions posed by the failure of regulation, and then of monetary policy to contain the economic turmoil, be understood with the cognitive tools currently available, or does there exist an opportunity for cognitive innovation (the possibility for transformation)? That is, given the commitment in the IMF to the efficacy of neoliberal economic ideas to what extent has it so far refrained from serious discussion regarding a potential shift to an alternative growth model, electing instead to respond within the intellectual frames that defined the orthodoxies of previous decades?

Answering this question should go some way towards determining the extent to which the failure of neoliberal economic ideas constitutes a progression towards a serious political-economic crisis (an inter-subjectively held consensus of the need for altered structures (change)). That is, although failure has seemingly de-legitimated existing economic models, new ideas can nevertheless be hard to accept and old ideas difficult to abandon.

Moreover, institutional structures not only nurture ideas and secure their propagation, they also protect and conserve them (Rueschemeyer, 2006:245). As a result, there exists the potential for future rules and regulations to embody past fallacies as any change, or continuity, remains inherently political (Abdelal et al, 2010:236). Existing institutions may therefore seek to protect dominant ideas, nip alternative ideas in the bud by the force of tradition, and assist vested interests so as to stop an opening for change; and they may hinder innovative ideas either for normative or material reasons (Rueschemeyer, 2006:244).

Similarly however, the preceding discussion demonstrates how moments of failure can throw causal interdependencies into doubt and open up alternative interpretations of economic problems which direct collective action in an altogether different direction. That is, moments of political-economic failure produce new lessons from which collectively we learn, and cultivate economic growth in new ways. These differences aside, 'whether new political or economic policies will emerge from the crisis, and what forms they may take are among the most important political and social questions' (Brand & Sekler, 2009:5).

In outlining how the IMF has interpreted the downturn, an assumption is made that responses are best understood as having progressed through a series of over-lapping yet distinct phases, with each requiring a different set of policy interventions and each having different implications for the neoliberal economic philosophy. This is an approach that has been increasingly deployed to make sense of, and better understand the nature and implications of, the current downturn.

Payne (2014) for example has done so in order to analyse the response of the G20 to un-ravelling events. Here, three stages are observed beginning in 2008 when the G20 called for coordinated global fiscal stimulus to stem the economic downturn in rejecting orthodoxy by calling on the deployment of the power and resources of the state. The second phase came in 2010 during which time according to Payne (2014:3) 'the politics of the crisis had changed in quite significant ways' as the neoliberal old guard began to strike back in response to the Keynesian policies advocated previously. The third phase however, came in 2013 as many observers suggested that, although effective during the first phase of the downturn, progress made by the G20 completely stalled.

This was an process deployed by Gamble (2014:51-75) who similarly suggested that the international economy has passed through four phases since 2007. The first of these, beginning in 2007 – 2008, ultimately led to the events of September and October 2008. The second phase was dominated by the recession in 2009 and the first signs of the recovery in 2010. In the third phase, the recovery was shown to be disrupted by over-zealous austerity and the euro-zone crisis in 2011 and 2012. The fourth phase, beginning in 2013, has been characterised by strong signs of a second economic recovery in Western countries.

In a broadly similar vein, a key assumption of this research is that the IMF response can be viewed as a multiphase event with each having important, albeit very different implications, for the neoliberal economic philosophy, problem definitions and policies. The first phase explored ran from summer 2007 until September 2008 and was linked to failures in the banking and financial sectors; the second phase came immediately thereafter as their effects spilled over into the real economy as monetary policy failed to stem its transmission and fiscal stimulus came to the fore; and the third phase was characterised by a shift in emphasis in 2010 as attention turned to the negative consequences associated with sovereign debt burdens, accrued as a result of fiscal interventions during the second phase.

Phase one: banking and financial sector implications

In July 2007 global credit markets deteriorated as a re-pricing of credit risk sparked increased banking and financial sector volatility and a broad loss of market liquidity. Initially, rising delinquencies on US subprime mortgages, in the context of a major housing correction led to a spike in yields on securities collateralised with such loans and led to a sharp widening in spreads on structured credits. Moreover, from mid-August, rising uncertainty about the amount and distribution of associated valuation losses and concerns about the off-balance-sheet exposures of financial institutions further added to market strains.

The result was a drying up of high-yield corporate bond issues, a sharp contraction in the asset backed commercial paper market, a dramatic disruption of liquidity in the inter-bank market, and stress on institutions funded through short-term money markets with three month interbank rates shooting up far in excess of policy targets. This occurred as banks sought to conserve their liquidity in the face of pressures to absorb assets from off-balance-sheet vehicles for which they were unable to obtain funding. Correspondingly yields on government paper declined sharply as investors looked for safe havens in which to invest.

Initial responses took two forms: policies to stabilize the financial system; and policies to prevent a repeat. In the case of the former, faced by mounting market disruptions, the WEO (2007:2-4) advocated that central banks in the major advanced economies: inject liquidity through open market operations to stabilize overnight interest rates; facilitate access to discount windows; and extend deposit insurance coverage to reassure depositors.

These interventions notwithstanding, the WEO (2007:6) noted that market liquidity would be restored in the following months as the inter-bank market reverted to more normal conditions. Adverse market developments were therefore considered ‘an inevitable return to greater market discipline after a period of very low risk spreads and lax credit conditions, which should ultimately strengthen the foundations of global growth’ (WEO, 2007:8-9).

As a result, the IMF continued to exhibit a large degree of confidence in the soundness of underlying economic fundamentals to such an extent that even as the banking and financial pathologies worsened, the WEO (2008:6) suggested that financial market turbulence would not significantly impact on economic activity. Rather, the suggestion was that growth would continue at a solid pace thanks to the strong balance sheets and capital positions of financial institutions, and the healthy situation in labour markets and house-hold net wealth.

As events worsened however, concern for macro-economic feedback effects grew thanks to reduced capital buffers and uncertainty about the size and distribution of bank losses. These combined with normal credit cycle dynamics to weigh heavily on household borrowing, the business environment, and asset prices, all of which combined to feed back into employment and output growth. As a result, the GFSR (2008:x) urged that monetary policy interventions should function as the first line of defence in combating the downturn.

In the case of the latter however, the GFSR (2008) highlighted a number of key themes that had contributed to banking and financial sector pathologies. These included: the fact that private sector risk management, disclosure, financial sector supervision and regulation all lagged behind innovation and the changing nature of risk models, thereby leaving scope for excessive risk-taking, weak underwriting, and asset price inflation; and a collective failure to appreciate the extent of leverage taken on by institutions and the associated risks of a dis-orderly unwinding. Crucially, these problems were not limited to the source of the down-turn (US) but, having played out to varying degrees elsewhere, suggested that weaknesses in risk management systems and prudential supervision were systemic in their nature.

It was therefore suggested that although there was a need to decrease financial system fragility, this should be conducted in such a manner that would not impede its efficiency through over-regulation. Indeed, given some of these initial conditions such as securitization and complex derivative securities 'should not and will not go away' (Blanchard, 2009:20) the challenge facing policy-makers at this juncture was understood as being to prevent the complexity associated with financial innovation from turning into dangerous opacity.

A fundamental part of remedying for this problem was, according to the MCMD (2009:3) the need for the collection and dissemination of more and better information and improved disclosure of risks (particularly 'off balance sheet risks') which had been largely limited due to legal constraints. Behind this was the notion that that risk could be correctly priced, but that markets were impeded from discovering these correct prices by information or incentive failures. Making information available to investors and counter-parties, it was thought, would be sufficient for them to assess the risks of their investments and would, by implication help to restore confidence by reducing uncertainty regards the prices of assets.

In a broadly similar vein, the GFSR (2008:xii) suggested that some of the ways the private sector could usefully contribute would be through: enhanced disclosure including providing timely and consistent reporting of exposures and valuations; disclosure strategies that would correct the risk management failings that may have contributed to losses and liquidity difficulties; and review distorted managerial compensation structures.

Taken together, these assumptions reflected the observation made in the GFSR (2008a:xiv) that, although the public sector had an important role to play, 'private sector financial institutions will nevertheless continue to play a crucial role in identifying and rectifying deficiencies in order to place financial intermediation on a more sound footing'.

Phase two: economic downturn

As 2008 progressed however threats to systemic stability increased, dislocations in securities markets intensified, and there were significant bank balance sheet adjustments and growing concerns about counterparty credit risks. One of the main channels for such macro-financial linkage was tightening bank lending standards in both the US and Western Europe as banks sought to decrease their leverage in the face of reduced market tolerance for balance-sheet risk, increasingly expensive bank capital, and reduced access to wholesale funding. These problems intensified financial strains which were beginning to take an increasingly heavy toll on economic activity (Baldacci & Gupta, 2009:1; WEO, 2008a).

This occurred despite central bank interventions in markets and IMF advocacy of aggressive policy easing and unconventional monetary policies (UMPs) such as bond purchases and forward guidance on the policy rate. Indeed, solvency concerns intensified, triggering banking and financial sector bankruptcies, forced mergers, and public interventions which led to a drastic re-shaping of the financial landscape and slowdown in economic growth.

Blanchard (2009:5-10) suggested that four factors related to the financial sector in particular had combined to turn a price decline into a broader economic downturn. Firstly, assets were created, sold, and bought that appeared much less risky than they were. Secondly, securitization led to complex and hard to value assets on the balance sheets of financial institutions. Third, securitization led to greater connectedness between financial institutions within and across countries. Fourth, leverage increased as financial institutions financed their portfolios with less capital. These consequences were amplified by the modern version of bank runs and the need by financial institutions to maintain an adequate capital ratio.

At this juncture the WEO (2008a:1) observed the downturn had 'entered a tumultuous new phase'. Similarly, in a 2008 interview Blanchard (2008:2) noted that 'the financial crisis has now evolved into a broader economic crisis, triggered by a freeze of the credit market, large wealth losses, and a loss of confidence', the result being a sharp fall in private demand. Indeed, such was its severity that Blanchard suggested that it could, in the absence of major policy interventions, exceed anything seen since the Great Depression in the 1930s.

As the downturn unfolded therefore, there was an assumption within the IMF that a purely market response was increasingly unfeasible. Indeed, piecemeal interventions to aid private sector strains had not succeeded in restoring market confidence and re-starting credit and money markets. Rather, financial market strains increased in an environment marked by declining asset values, exacerbated by pro-cyclical forces such as ratings downgrades, the challenges of distinguishing good from bad assets, and strong from weak institutions, all of which were combing to spill over to, and adversely affect, the real economy.

Although during the first phase, there was still very much a sense within the IMF that the broader economic context could be characterised by increased uncertainty, as the second phase progressed it became increasingly evident that, given what the WEO (2009) termed 'an exceptionally uncertain environment', evidenced by the inefficacy of status quo policies and institutions to prevent a more severe economic downturn, that a substantive shift in the kinds of policies advocated by the IMF thus far would be required.

The GFSR (2008a:50) therefore noted that if a resolution was to be achieved that limited damage to the financial system and broader economy, 'the authorities will need to play a major role in it', the ultimate goal being to mitigate the feedback loops between the financial system and the broader economy. In this regard, Blanchard and Vinals (2008:xii) suggested that, although private sector solutions continued to be preferred, emergency government fiscal policy interventions 'must play a crucial part in providing short-term support to the global economy'. At this juncture there was therefore a clearly observable political economy which, in contrast to the first phase, recognised that market responses alone would be insufficient and that the resources of the state would need to be deployed.

Although largely eschewed as a policy approach within the IMF, its advocacy was justified in light of research presented in the October 2008 WEO. This observed that past episodes of financial stress involving shocks to the banking sector are typically followed by deeper than usual business cycle downturns and more protracted recoveries as the main transmission channel from financial sector shocks to downturns in activity was a contraction in net lending to the business and household sectors.

Phase three: sovereign debt crisis

By the latter part of 2009 and particularly into 2010 however, there was a definite sense within the IMF that, following the implementation of unprecedented policy actions, although potential downside risks still existed, the global economy had turned a corner (see for example, GFSR, 2010; WEO, 2010). This was characterised most evidently by the rebounding of financial markets; banks raising capital once again; and wholesale funding markets reopening; all of which contributed towards the abatement of extreme tail risks.

At this juncture the attention of the IMF turned from the fiscal support advocated during the second phase to the transfer of financial risks to public balance sheets, which, combined with the financial burden of fiscal stimulus 'raised concerns over crowding out the private sector and the sustainability of public sector finances' (GFSR, 2009a:xv). The concern here was that record sovereign debt issuance could push up interest rates, exacerbate short-term strains in funding markets as investors required higher yields to compensate for potential future risks, thereby limiting room for policy manoeuvre in many advanced economies, and hurting the nascent recovery. As a result, an assumption was made that deteriorating public finances could compromise sovereign creditworthiness.

Indeed, by the early part of 2009 a Staff Position Note by the Fiscal Affairs Department (FAD) noted that economic downturn was 'having major implications for the public finances of most countries' (FAD, 2009a:3). It was therefore suggested that discretionary fiscal stimulus, although cushioning the global economy from the worst effects of the downturn, was nevertheless giving rise to a fiscal deterioration that was especially strong for advanced economies, where the increase in debt and contingent liabilities was on as pervasive and a scale not seen since the end of the Second World War. Indeed, government debt was projected to rise by 20 percent of GDP in 2008-09 alone (FAD, 2009a:3). This fiscal outlook raised issues of fiscal solvency which had the potential to trigger adverse market reactions.

These vulnerabilities, according to the GFSR (2009:xv) 'underscored the need to... reduce the private risks now borne by sovereign balance sheets'. It was therefore suggested that countries should mitigate this risk by designing, articulating, and communicating medium-term fiscal consolidation plans that take into account their financial sector stabilization policies and contingent liabilities (GFSR, 2009a; GFSR, 2010). These, it was suggested, should include clear time-frames to bring down gross debt-to-GDP ratios over the medium term as well as contingency measures if the deterioration in public finances was greater than expected. Here therefore there was a perceived clear alteration in the global risk profile.

An assumption was therefore made at this juncture that most advanced economies should embark on fiscal consolidation in 2011. Although the IMF noted that the pace would vary depending on country circumstances, the suggestion was that for countries facing large increases in risk premiums, and where urgency was greater, consolidation would need to proceed immediately, and at a slower pace for countries with sufficient fiscal space.

As a result, the problem presented by the third phase of the downturn appeared to have presaged a shift back towards the kinds of neoliberal policies advocated by the IMF previously. Firstly, the calls for a retreat from fiscal stimulus echoed prior assumptions that the appropriate role for fiscal policy was solvency and sustainability. Secondly, the IMF advocated a series of adjustment policies that would provide an enabling framework in which growth would once again flourish. This included the need to address aging-related pressures which, if left un-addressed, had the potential to dwarf the fiscal costs incurred by the downturn; and labour market reforms which would contribute towards a growth-friendly environment (see for example, Blanchard & Vinals, 2010:xii; GFSR, 2010:xii).

Concluding remarks

This chapter has sought to provide a background with which to understand the origins and causes of the current downturn. In doing so, two points were made. On the one hand, it has been demonstrated that, having been variously conceptualised as the result of failures specific to the policy realm, the economic ideas steering global economic governance were not understood as being fatally flawed and that minimal tinkering was all that was required to restore an otherwise effectively functioning political-economic system back to normalcy.

On the other hand it was suggested that two policy areas synonymous with the neoliberal economic ideas underpinning global economic governance were fundamentally implicated in the downturn. It was therefore asserted, in a manner consistent with Wilson and Grant (2011:6) that the dominance of the neoliberal economic ideas at the start of the downturn were not mere coincidence 'but rather the GFC was the result of them'. Consequently, the downturn could be more appropriately interpreted as a crisis *of* neoliberalism its self.

It was therefore assumed that at a minimum, neoliberal economic ideas had been at least, if not considerably more, discredited than Keynesianism had been in the 1970s. As a result, it was a commonly-held assumption that we should similarly have anticipated that so too would the current failure of neoliberal economic ideas bring about changes in political coalitions, policy thinking, political strategy, and ultimately, political change.

Secondly, this chapter has demonstrated how the downturn can be best understood as a multiphase process with each drawing attention to a particular interpretation of the prevailing problem. The following chapters, drawing on the phases outlined here, explores the implications for the prevailing neoliberal economic philosophy, problem definitions and policy priorities in the IMF with reference to monetary and fiscal policy, and financial sector liberalization and deregulation.

In doing so it is demonstrated that, during its first phase, perceptions regarding the efficacy of the neoliberal economic philosophy were not implicated to any significant degree as the downturn was interpreted through existing frames of reference. As a result, the kinds of policies advocated by the IMF continued to be justified in line with current expectations.

During its second phase however, the global economy had become so uncertain that there was a recognition within the IMF that much of what it thought it knew about economic policy and financial sector liberalization and deregulation had been fundamentally challenged and that substantive reform in a number of areas would be required.

This notwithstanding, a key assumption of this research is that, as the downturn entered its third stage, (a shift in focus to the implications of soaring sovereign debt burdens) it became increasingly evident that many of the policies advocated during the most acute phase (the second phase) had been simply deployed in order to save neoliberal economic ideas from its follies rather than being representative of a more significant shift.

As a result, it is demonstrated in the chapters that follow, consistent with Hay (2010, 2013), that despite the severity of the failures of neoliberal economic ideas, it is not yet possible to talk of a broader crisis *of* neoliberalism in the IMF as this would require that actors inter-subjectively interpret neoliberalism as being responsible for the turmoil. The following chapters show however that as yet, there is very little evidence to suggest that this is the case.

Chapter 4

Economic Policy I

'There is no perfectly static state in the history of life. Change is the norm.'
(Orion Lewis and Sven Steinmo)

Introduction

In 2008 the IMF deferred to prevailing neoliberal economic ideas in its advocacy of the deployment of a range of conventional, and latterly, unconventional monetary policies (UMPs) in an attempt to contain the economic downturn brought about by turbulence in Western banking and financial systems. Given their inability to successfully do so however, the IMF broke with orthodoxy and 'for the first time in its history, called for a global fiscal expansion across all countries' (Cottarelli, 2013:1) to help stimulate aggregate demand, and in doing so, deferred to a distinctive political-economy privileging state intervention. This was a move interpreted at the time as having the opportunity to usher in a potentially epoch-shaping shift in the neoliberal economic ideas steering IMF policy actions.

Chapters 4 and 5 chart this ostensible shift and the implications for neoliberal economic philosophy in the IMF. They do so through a text analysis of research produced by knowledge-based experts within the IMF who have 'published a series of reports and papers... with the aim of contributing to the broader public debate' (Moschella, 2010:136).

On a broad level the in-house bi-annual publications World Economic Outlook (WEO) tracking short and medium term global economic developments; and Global Financial Stability Report (GFSR) created with the intention of strengthening IMF surveillance of developments in financial markets (GFSR, 2002:iii), provide the broader context within which to explore the interpretation of, and initial responses to, the downturn.

More specifically however, the following two chapters draw on research produced by the Fiscal Affairs Department (FAD) of the IMF. This includes the bi-annual Fiscal Monitor which was created in the aftermath of the economic downturn to track fiscal responses and provide policy advice; and IMF Working Papers, Policy Papers and Staff Position Notes produced by FAD Department Director Carlo Cottarelli, senior officials Emanuele Baldacci and Antonio Spilimbergo among others, and Research Director Olivier Blanchard.

These publications are crucial sources of investigation as they attempt to influence the broader public debate in a manner consistent with existing economic ideas. This is the "high" data of policy documents/statements that circulates among elite institutions, policymakers, academics and the media as part of a broader communicative discourse. Its incorporation allows for the opportunity to track initial IMF interpretations and responses to the unfolding turbulence and the kinds of policies considered necessary (Weldes, 2006:178).

Moreover, acting as an important supplement to this research, this chapter and the next also incorporate the means by which knowledge is communicated through the speeches of major public figures of the IMF to a broader audience. That these are similarly rife with, and help to instantiate, dominant neoliberal economic ideas makes it possible to track IMF representations of the downturn and associated policy responses. This includes speeches by Managing Directors Dominique Strauss-Kahn and latterly Christine Lagarde, First Deputy Managing Director John Lipsky, Research Director Olivier Blanchard and FAD Department Director Carlo Cottarelli. Against this backdrop, this chapter proceeds as follows.

Firstly, the chapter details the unravelling of the downturn which, limited in its first phase to the banking and financial sectors (understood here as ranging from summer 2007 to autumn 2008), was largely restricted to concerns related to a decline in mortgage markets, deteriorating liquidity in financial markets and only a general slowdown in economic activity. In a manner consistent with prevailing neoliberal economic ideas, the IMF called for the deployment of monetary policy as the first line of defence in the form of interest rate cuts, and, thereafter, unconventional monetary policies (UMPs) in the form of central bank interventions into money markets. Therefore, during the first phase, the IMF is shown as being characterised by a considerable degree of continuity in the policy interventions it advocated, which although increasingly unconventional, continued, by and large, to be derived from neoliberal frames of reference.

Secondly, the chapter demonstrates how, given both the inefficacy of conventional and UMPs to prevent the spill over of the downturn into the real economy, (the second phase beginning in autumn 2008) the IMF broke with orthodoxy in advocating a range of policy interventions that stood in contrast to those associated with neoliberal economic ideas, most notable among which was the call for globally coordinated fiscal stimulus. In doing so, it is demonstrated how these interventions, in more closely resembling those economic ideas associated with Keynesianism, led to the suggestion that the severity of the downturn might precipitate a significant shift in the economic ideas steering IMF policy priorities.

This notwithstanding, Chapter 5 demonstrates that this shift never materialised for the simple reason that the IMF never abandoned its faith in the efficacy of the neoliberal economic philosophy. Rather, fiscal stimulus was deployed in order to save neoliberalism from its follies, not act a pre-cursor to major change, to suggest otherwise would be to misinterpret the intentions of the IMF at the time. Indeed, it is demonstrated that during the third phase (beginning in late 2009/early 2010) as attention turned to soaring sovereign debt burdens, the IMF not only called for major fiscal adjustment, but the entrenching of a host of policies consistent with the neoliberal economic philosophy and problem definitions.

Phase 1: Monetary efforts to shore up the banking and financial sectors

It was assumed that an approach to economic management centred on monetary policy had helped foster a considerable degree of economic stability characterised by low inflation and steady economic growth. This led to an overwhelming optimism within the IMF that an economic environment typified by severe economic disorder had been largely eradicated.

So entrenched had this assumption become that, despite problems in the US economy in 2007, such as rising stress in the sub-prime mortgage market and signs of deterioration in Alt-A mortgages – those that lay somewhere between prime and sub-prime - (and which could impact on the broader housing market), the WEO (2007:2) suggested that global economic risks remained largely encouraging, demonstrable in fast global economic growth.

Paradoxically however, at the same time the IMF was lauding the apparent stability of the financial system, market disruptions were becoming increasingly pronounced, characterised by a re-pricing of credit risk which sparked further financial volatility and a loss of liquidity. This added to uncertainty regarding structured product's valuations which led to 'rating migration', thereby channelling uncertainty to a broader range of products, and leading investors to demand wider spreads to compensate for uncertainty about how risks were managed and allocated (GFSR, 2007a:1). Moreover, banking and financial sector pathologies extended, albeit only marginally at this stage, into a slowdown in broader economic activity.

Indeed, as 2008 progressed, further losses, falling asset prices, and a deepening economic downturn contributed to serious doubts about the viability of a broad swath of the financial system. Deleveraging accelerated and become disorderly – marked by a rapid decline in financial institutions' share prices, higher costs of funding, and depressed asset prices. The result was the failure of institutions as markets became unwilling or unable to provide capital or absorb assets, thereby creating a near lock-up of money markets (GFSR, 2008a:xi).

Moreover, macroeconomic feedback effects grew as uncertainty about the size and distribution of banking and financial institutions' losses, along with normal credit cycle dynamics weighed heavily on business investment and household borrowing, in turn feeding back into output growth and employment. As a result, the GFSR (2008:1) cautioned that 'the potential for a significant economic slowdown' had increased substantially.

Problem definition

The capacity of the IMF to deal with the sheer volume of information generated regarding the form and severity of banking and financial sector pathologies, along with their potential impact on economic growth was inherently limited. As a result, the IMF deferred to existing schemas - a 'subjective "theory" about how the social or political world works' (for our purposes here, neoliberal economic ideas) so as to 'order, interpret, and simplify' (Khong, 1992:13) the unfolding economic downturn. That it did so reminds us that the IMFs initial response to the downturn 'must be understood as social, political, and ideological' (Snyder, 1991:14) as opposed to being considered part of a rational response to external stimulus.

Operating on the assumption therefore that the IMF did not respond to unravelling events in an obvious and predictable way but that the ideas held 'profoundly shape the way external demands or shocks are interpreted' (Barnett & Finnemore, 2004:9), the corollary was that neoliberal economic ideas held by the IMF carried with them default settings for variables which privileged the elucidation of information consistent with existing ideas, and provided a proto-type against which specific examples and lessons from previous economic downturns could be drawn. In highlighting this process, an acknowledgement is made, consistent with Blyth (2002:26), that it was the economic ideas held by the IMF that played a critical part in helping to reduce the increasing political-economic uncertainty.

Noting this allows us to demonstrate how these ideas shed light on and provided the basis by which to relate to the downturn, and how, hamstrung by existing economic orthodoxy, the analogies invoked and lessons learned ultimately proved inadequate in themselves to prevent a much more severe economic downturn (Snyder & Diesling, 1977:293).

Drawing on these economic ideas, during the first phase of the downturn, the IMF drew on the lessons of the past (or what they thought those lessons taught them, its self an entirely subjective exercise) to reduce the uncertainty and guide their initial response. In particular, a number of assumptions were made (implicit or otherwise) through reference to historical analogies that compared the unfolding economic downturn to others that had preceded it.

In doing so, the IMF sought to invoke the lessons of the past so as to display the unravelling economic environment as one characterised by measurable risk as opposed to uncertainty (Knight, 1957:215). Indeed, by drawing on the lessons of previous economic downturns we show how the analogies invoked suggested that at that juncture, events, being comparable with a larger group of similar instances from the past, were more knowable. This meant the downturn could be more readily characterised as a situation of risk rather than uncertainty which is so unique as to be not readily assimilated with a larger number of like-instances.

The means by which this was undertaken can be explained through reference to the schematic provided by Khong (1992) outlined in Chapter 1: *AX:BX;AY:BY*. In this instance however *A* (the economic downturn) was interpreted as analogous to event *B* (the dot.com boom for example) in having characteristic *X* (a downturn brought about by an asset boom and bust); *B* had characteristic *Y* inasmuch as it was viewed resolvable through monetary policy interventions, namely, a reduction in the policy rate to stimulate economic activity. So too therefore was it thought that *AY* (the current economic downturn brought about by an asset boom and bust) was resolvable through a similar set of policy interventions.

Lessons learned from the past in the form of historical analogies (themselves a derivative of the frames provided by neoliberal economic ideas) can be understood as interpretive devices called upon by the IMF to perform three tasks which help us understand why initial responses took the form they did. Firstly, they played a diagnostic role in defining the nature of the problem by comparing unfolding events with previous instances with which the IMF was more familiar. The second and third followed this diagnostic by outlining the stakes involved and implied necessary solutions to the problem so-defined (Khong, 1992:20).

On the basis of the preceding discussion we can see how the economic downturn generated a number of simplifying expectations about its nature, which, viewed as analogous to others, meant it could be treated in a similar manner. In particular, two inferences both guided the IMFs response, and sought to persuade member states that the overall global economic environment could still be characterised as one of risk as opposed to uncertainty.

Firstly the WEO (2007:xii) noted that the chances of local disturbances resulting in global spill-over's were low as history showed that slowdowns were rarely attributable to country- or sector- specific developments, but occurred when an event adversely affected a number of countries simultaneously. Further mitigating for this potential, it was noted that: house-hold finances were in a solid position; equity gains over the last year returned household net worth to previous peaks; and low interest rates led to reasonable debt-servicing costs.

Secondly, and most pertinently, it was noted that forward-looking monetary policy would reduce the output effects from any potential shocks just as it had done during previous economic downturns, such as the dot.com boom and subsequent bust. This reflected the "lean versus clean" (Blanchard et al, 2013:3) assumption that it was better to clean the mess left by a bubble bursting through reductions in the policy rate than it was to lean against bubbles which were inherently difficult to track and thereafter to effectively counter.

The September 2007 WEO perhaps best exemplified the IMFs confidence in these simplifying assumptions by not only exalting their efficacy, but in positing that, thanks to advances in our economic knowledge, their success was without historical precedence.

In particular, it was noted that: institutional quality had led to greater political and economic stability in policymaking; better macroeconomic policies dampened output fluctuations; more developed financial systems had smoothed consumption and investment plans; and the increased durability of expansions reflected long-term sources. Against this backdrop, the potential for severe economic dislocations of the type played out in the past were considered, if not entirely precluded, then certainly only minimal (WEO, 2007a:Ch5).

Given these assumptions, banking and financial sector volatility in 2007 and into 2008, along with an associated slowdown in economic activity, were interpreted by the IMF as nothing more than a modest correction to rising asset prices as opposed to a fundamental change in market sentiment. Rather, the unfolding turbulence was understood as being rooted in weakening credit discipline, increased financial sector leverage and investor complacency.

This demonstrates the impact that learning the lessons of the past by interpreting events through existing economic ideas had on influencing the manner in which banking and financial sector pathologies, and the economic downturn were initially diagnosed, why responses took the form they did, and why the downturn was so readily interpreted and constructed by the IMF as a crisis *for*, rather than *of,* neoliberal economic ideas.

Policy priorities

Against this backdrop, existing beliefs continued to provide the underpinnings of a shared account of the nature of the functioning of the economy and framed initial policy responses to the downturn in a manner consistent with existing economic orthodoxy, most notably regards the perceived efficacy of conventional monetary policy interventions.

This was exemplified in a 2008 speech by Strauss-Kahn (2008) who urged that monetary policy should continue to operate as the first line of defence to stave off a greater downturn in the real economy. The 2008 WEO (2008:38) echoed this call in suggesting that, in the US and EU, uncertainty about the impact of financial turbulence and the deterioration in labour market conditions justified 'rapid interest rate cuts and a continuing bias toward monetary easing until the economy moves to a firmer footing', despite relatively high inflation.

This completely contradicted the policy advice given to developing countries which was in 'general agreement that when asset prices fall sharply – for example, after the bursting of an asset price bubble – monetary policymakers should react promptly and aggressively to contain inflation and stabilise output' (WEO, 2008:122) through policy rate *rises*.

This is exactly what the IMF had advocated to developing countries during previous financial crises such as that in Asia (see Chapter 2), deemed as it was, necessary to stem capital outflows regardless of the consequences for businesses that might be at risk of closure if they were even only moderately leveraged (Stiglitz, 2002). Indeed, Strauss-Khan (2008:4) again suggested that emerging economies 'will need to raise policy interest rates in line with rising risk premia to stem outflows and bolster confidence in their currencies'.

Although this suggested advanced country exceptionalism, interest rate cuts were justified for advanced economies by the IMF as, although inflation was rising at its fastest pace since the 1990s (Lipsky, 2008:3), it was noted that 'measures of *underlying* inflation – price indices excluding food and fuel prices, inflation expectations, and labour costs – have been broadly contained' (WEO, 2008a:4, emphasis added). Moreover, the WEO (2008a:21) noted three trends would mitigate inflationary risks in advanced economies that were not applicable to developing economies: real wage flexibility; more secure anchoring of inflationary expectations by vigilant central bankers; and declining energy use and economic activity.

As 2008 progressed however overall risks increased as the downturn spread to cross-border credit and funding markets, exacerbating anxieties of the impact that the reversal of the housing boom on financial markets and systemically important financial institutions. More-over, the deterioration of credit injected greater uncertainty into the financial system, the outcome of which was to curtail inter-bank liquidity, weaken capital adequacy, and prompt a re-pricing of risk, the result of which was increased demand for central bank liquidity.

Against this backdrop of market-wide funding pressures and the inability of conventional monetary easing to stem the unfolding turmoil despite the fact that policy rates were at, or near to, the zero lower bound (ZLB), the IMF called for the deployment of a range of UMPs to prevent a serious financial meltdown. In doing so, calls were made for central banks to inject liquidity into money markets in order to increase the volume of long-term financing and provide standing credit facilities. The argument that states should confine themselves to providing a steady, stable increase in the money supply consistent with long-term growth was clearly abandoned in the face of the unfolding turmoil. Nevertheless, these measures did have monetary policy implications, analogous as they were to central banks' traditional roles of lenders of last resort as they aimed to both combat financial system dysfunction (including runs and multiple equilibria) and prevent an even greater collapse of confidence.

Although the over-arching goal of monetary authorities therefore remained unchanged, the instruments adopted were unconventional in their breadth and scale as unprecedented liquidity was provided to a broader set of recipients, and with a wider aim, to support market functioning. Therefore, at this stage, although termed unconventional, the policies retained many similarities with conventional monetary policy as the fundamental objectives remained unaltered: namely, to support price and financial stability (IMF, 2013a:6-7).

The deployment of first round UMPs notwithstanding, as 2008 progressed further financial sector losses, falling asset prices, and a deepening economic downturn contributed to an even deeper sense of financial sector mayhem, manifest in a rapid decline in share prices and increased costs of funding. The result was the failure of institutions, increasing concern regarding counterparty risks, and a near lock-up of global money markets (GFSR, 2008a:xi).

Again, the IMF acquiesced to its advocacy of the deployment of monetary policy, with Lipsky (2008) suggesting that the first line of defence remained with monetary authorities who would continue to play a critical role in helping economies find their footing. Nevertheless, the inability of conventional monetary policy and UMPs to prevent events from continuing to deteriorate provided the motivation for calls within the IMF for a second round of UMPs (Strauss-Kahn, 2009b). These policies, still monetary in their nature were unlike in their first guise unconventional in their instruments and operational targets as central banks resorted to forward guidance in the policy rate, and even less conventionally, to bond purchases.

On the one hand, forward guidance on the policy rate was communicated to market actors and signalled a shift in policy to maintaining low rates for a longer period than would have been warranted by central banks' usual reaction functions. On the other hand, large-scale asset purchase programmes (LSAPs), a process of buying up bonds, was advocated to reduce the stock of longer-term bonds in investors' portfolios, inducing them to accept lower returns to hold scarcer assets. The assumption was that LSAPs would reduce interest rates along the term structure which would contribute towards stimulating economic activity.

Although these policies were increasingly unconventional, such was its continuing belief in the ability of neoliberal economic ideas to prevent a more serious collapse, the IMF continued to reason through historical analogy that past episodes of financial stress such as that being played out had not had a major impact on economic activity as segments of the financial system were, in part, able to compensate for difficulties in others. Moreover, historical evidence, it was noted, showed bank lending rose during expansions and declined during contractions while conversely, the price of bank credit rose during a slowdown, imbuing banks to tighten lending standards (with the opposite being true during an upturn).

Indeed, the WEO (2008:9-16) noted that 'current changes in lending standards, demands, and spreads were exhibiting patterns in line with historical experience', an assertion which contributed to the IMF's interpretation of the unfolding turbulence as a credit squeeze as opposed to a more serious credit crunch. Reasoning by historical analogy and diagnosing the turbulence like so constituted an attempt to reduce the uncertainty generated by banking and financial sector pathologies by linking them with a series of ostensibly similar events.

However, this was an inherently political exercise. It was a process employed by the IMF as a means by which to define a series of disparate events as being analogous to others that have preceded it. This search for repetition was therefore key because it allowed for relative continuity in the policy realm, thereby promoting a sense of certainty about the future, regardless of how accurate a depiction of the unfolding turbulence this might have been.

Indeed, the diagnosis of the unfolding downturn in its initial phase, not historically dissimilar from previous downturns, meant the policy interventions advocated by the IMF, even at this stage, continued to be drawn from existing neoliberal frames of reference. Consequently, the IMF continued to exhibit faith in central bank interventions to remedy for unfolding pathologies by suggesting that they were neither paradigmatic nor institutional.

Indeed, this interpretation of the downturn as a moment of instability puncturing an otherwise stable economic environment led Lipsky (2008:6-7) in a 2008 speech to suggest even at this juncture that a more serious downturn could still be avoided. This was premised on the assumptions that: declining oil prices were contributing to a reversal in adverse terms-of-trade effects and the erosion in purchasing power, and real wages being felt in most advanced economies; the US housing market would bottom out during 2009 allowing affordability measures to return to levels consistent with past experience; while credit conditions were tightening in the US and Europe, IMF analysis highlighted that a slowdown in credit provision need not forestall an economic recovery; and resilient domestic demand and growth in emerging economies would make an important contribution to global growth.

Implications of lessons from the past for continuity in neoliberal economic ideas

We would certainly not expect that the neoliberal economic ideas through which incoming information was interpreted during the first phase of the downturn be abandoned by the IMF at the first sign of discrepant information. Indeed, Jervis (1976:159) has suggested that if every observed anomaly were taken at face value 'research would instantly degenerate into a wild-goose chase after imaginary fundamental novelties'. In a similar vein, Hay (2008:69) notes that the earliest phases of political-economic failure are 'more likely to result in the vehement reassertion, expression, and articulation of prior conceptions'. This suggests that, during the initial onset of the downturn, there were good reasons for the IMF not to abandon its commitment to neoliberal economic ideas in the face of events.

Indeed, to take on board incoming information through an alternative set of economic ideas would not only constitute an admission that the IMFs expectations were mistaken in major respects, but also that problem definitions and policy prescriptions either had failed, or were destined to do so. Particularly given that neoliberal economic ideas have become accepted to varying degrees the world over (Payne, 2005) these are difficult admissions to make and help us understand why initial responses took the particular form they did.

Viewed in such a manner, it would not be accurate to suggest that in the earliest stages of the economic downturn the IMF could automatically 'be condemned for cognitive distortion or self-defeating blindness' (Jervis, 1976:172). Nevertheless, the key point here is that as the first phase progressed, as banking and financial sector pathologies intensified and the economic downturn progressed, incoming data and policy responses were increasingly stretched to fit with existing economic ideas, a process exemplified by the advocacy of a range of UMPs. As a result, the IMF's ability to correctly identify the mounting risks 'was hindered by a high degree of groupthink, intellectual consistency, and a general mindset that major financial crises in large advanced economies were unlikely' (BWP, 2011:1).

This was not a trait exclusive to the IMF, but in many respects reflected the problems associated with interpreting incoming information through the lens provided by existing economic ideas, the implications this had for drawing on lessons from the past by reasoning through historical analogy and why they are more often that not used sub-optimally (Khong, 1992; Jervis, 1976; May, 1974; Snyder, 1991). Three reasons are especially noteworthy.

On the one hand, we can see in this instance how the analogies invoked and lessons learned – the assumption that, just as monetary policy interventions had been sufficient to stem previous downturns in advanced economies so too would they be sufficient again - were selected on the basis of what were in fact incredibly superficial surface similarities.

The outcome was that the kind of conclusions drawn form IMF interpretations about what the downturn meant, and what policies could be considered appropriate, were inherently limited and ultimately insufficient to deal with its particularities. Indeed, not probing more widely in search of alternative analogues meant that less obvious but perhaps more relevant lessons may have been derived. However being guided by superficial similarities, themselves the result of adherence to neoliberal economic ideas, meant the scope for misinterpreting incoming data increased substantially (Snyder & Diesling, 1977:317; Jervis, 1976:191).

The problem with this approach therefore was that the initial downturn was conceptualised as 'merely a moment of instability puncturing an otherwise stable financial environment with a temporary mishap' (Brassett et al 2010:1) which prevented the potential for an earlier diagnosis of a signal event highlighting deeper changes and probable contradictions, tensions and fallacies inherent to the neoliberal economic ideas guiding IMF actions.

On the other hand, by drawing on what were only superficial surface similarities, incoming information continued to be assimilated in line with extant neoliberal economic ideas. This demonstrates why IMF staff was more receptive, and sensitive to, incoming information consistent with the neoliberal economic ideas they held and the analogies they invoked.

The corollary of this however was that discrepant information that would have pointed towards a more serious downturn was marginalised given the reluctance to accept evidence contrary to existing expectations. Rather, an attempt was made to 'fit new information into... patterns of expectations' (Snyder & Diesling, 1977:325). Indeed, retaining their belief in the efficacy of neoliberal economic ideas in the face of seemingly discrepant information suggested that, despite appearing otherwise, the basic theory continued to hold true.

By adopting this approach, information that did not fit was slighted, ignored or twisted to confirm (or at the very least not contradict) neoliberal economic ideas and their validity. This was a scenario inherent to interpreting information through the lens of existing economic ideas: they often persist stubbornly even in the face of evidence contrary to their normative and cognitive underpinnings; and shows how the past was considered such a strong guide for future action that great faith continued to be placed in their capacity to guide policymakers of the appropriate means by which to rid for unfolding pathologies. The consequence however was that instead of correct perceptions, the IMF was characterised by increasingly 'strained interpretations and tortuous arguments' (Jervis, 1976:154).

As a result, although there exists no clear metric by which to determine the point at which holding on to existing neoliberal economic ideas becomes disparaging discrepant information beyond a point of reasonable comprehension, it was increasingly evident that as the first phase unravelled IMF policy responses had become increasingly incapable of dealing with the particularities of the economic downturn, despite its evident defects.

Finally, the implications of adhering to lessons from the past was that the analogies drawn, by slighting or ignoring information that ostensibly contradicted them, meant that the IMF was predisposed to particular courses of policy action consistent with prevailing neoliberal economic ideas as opposed to one of the many other options that were available.

By electing not to do so, the analogues invoked and lessons learned by the IMF meant that policies - hamstrung by existing economic ideas and limited by what was considered appropriate - not only failed to illuminate the uniqueness of the downturn, but also led to policy actions which would prove insufficient to stem the flow of banking and financial sectors pathologies from having major adverse consequences for the real economy.

Indeed, the kinds of policies advocated increasingly involved violations of generally agreed rules for treating economic downturns, most notable among which were unconventional monetary policies as conventional monetary policy easing was hindered by the ZLB. Nevertheless, that the IMF continued to hold onto such ideas in the face of contradictory evidence of the utility of an exclusively monetary policy approach to managing the downturn leads us to conclude that the approach taken was becoming difficult to justify.

This demonstrates how, drawing on the constructivist assumption that moments of political-economic failure require being interpreted and diagnosed *as* a crisis through discourse and changes in the way situations are defined, there was no attempt by the IMF to define the economic downturn in such terms. That is, there was no direct sense of crisis as attempts were made by the IMF to continue to posit the efficacy of prior economic ideas and policies.

The preceding discussion therefore leaves us well placed to state that despite the advocacy of monetary policy in both its conventional and unconventional guises, the economic down-turn did not fundamentally challenge the efficacy of the neoliberal economic philosophy in the IMF during its first phase. Rather, policy responses were consistent with those provided by neoliberal economic ideas as monetary policy and central bank interventions continued to assume prominence as the first line of defence despite the declining economic downturn.

Nevertheless, it is demonstrated hereon in that during the second phase (beginning in autumn 2008), despite piecemeal adjustments, and with increasing evidence of the inefficacy of existing problem definitions and associated policy prescriptions, sufficient negative evidence accumulated 'to disorganise the original neat pattern of expectations' (Snyder & Diesling, 1977:325). Therefore, although the IMF had initially clung onto extant expectations, these appeared to be significantly destabilised during the second phase.

Phase 2: Fiscal efforts to shore up the 'real' economy

Although in its first phase pathologies were largely limited to the banking and financial sectors, it was noted as early as the April 2008 WEO that macroeconomic feedback effects were a growing concern as the size and uncertainty of bank losses, and normal credit cycle dynamics were likely to weigh heavily on house-hold borrowing and business investment, in turn, feeding back into employment and output growth. However, no suggestion was made of the need for major globally-coordinated fiscal interventions into the economy. Rather, consistent with neoliberal economic ideas, it has been demonstrated that monetary policy and central bank interventions continued to be advocated as the first line of defence.

Nevertheless, by the autumn of 2008, it was clear that monetary policy and central bank interventions alone would be insufficient to stem the banking and financial sector failings and prevent the economic downturn from worsening further. Rather, in developed economies policy rates were already at, or close to, the ZLB so there was no scope to reduce them further. Indeed, the economic environment had become so uncertain in terms of what the IMF thought it knew regarding monetary policy that events now forced 'the re-examination of intentions, of conceptions about how the world works' (Seabrooke, 2008:2).

At this juncture, the IMF was therefore faced with a situation that went far beyond a still knowable economic environment that could by any reasonable proxy be characterised by risk. Rather, as the second phase unfolded it was evident that the economic environment was in fact characterised by considerable uncertainty, a situation in which it had become impossible to form a similar group of instances on which to draw (Knight, 1958:253). That is, the IMF was faced with a fundamental uncertainty in forming expectations the consequence of which was that it was impossible to make probabilistic calculations of events as their ability to form meaningful estimates of future events diminished (Widmaier et al, 2007:750).

Indeed, the declining performance of status quo institutions and policies destabilised inter-subjectively held beliefs regarding the efficacy of monetary policy as the primary (or only) tool with which to manage economic downturns. On the substantive dimension it therefore became harder for the IMF to cognitively justify the prevailing set of economic ideas and associated policy prescriptions in terms of their interest-based logic and necessity. That is, if cognitive ideas demonstrate how policies offer solutions to problems, how problem definitions define the problems to be solved and identify the methods by which to solve them, clearly prevailing cognitive ideas had proven ineffective at dealing with the downturn.

This was especially evident at the end of 2008 as plummeting domestic demand made it apparent that the unfolding turmoil was more than a simple downturn in the sub-prime mortgage market and a liquidity event. Rather, banking and financial sector pathologies precipitated a fall in aggregate demand to such an extent that the global downturn was interpreted as having the potential, if unchecked, to exceed anything seen in recent history.

It was therefore apparent that although monetary policy (both conventional and otherwise) would continue to be critical in meeting policy challenges, it had proven in its self in-sufficient to prevent the downturn from worsening further. That is, low rates had become un-responsive (akin to pushing on a string) as the fundamental underlying engines of the economy were unable to exert any kind of a significant pull (Strauss-Kahn, 2008a:1; 2008b).

It was against this backdrop that, in a 2008 interview Blanchard noted that in the absence of more significant intervention, we may see some of the vicious cycles observed in the past. These concerns were manifest regarding the transmission of the downturn from the banking sector to the real economy and were exacerbated by worries that a further fall in demand would lead to an increase in risk that deflation, rising debt, and feedback loops to the financial sector may materialise, thereby contributing to already pessimistic expectations.

During the onset of crises in developing countries the IMF called on national authorities to implement 'a substantial rise in interest rates' to make it more attractive to hold domestic currency, and fiscal adjustment to 'cover the carrying costs of financial sector restructuring' (Fischer, 1998:170-171) and stabilise the balance-of-payments, ease external adjustment, and bolster market confidence (Chari & Henry, 2013:8-9). This was consistent with IMF assumptions that 'positive confidence effects could dominate the adverse mechanical effects of cuts in spending or increases in revenues, thereby leading to 'expansionary fiscal consolidation'' (IMF, 2013b:20; see also Davies, 2006).

These policy interventions were informed by a significant body of research in the IMF which suggested that discretionary fiscal policy had only a limited role to play in managing downturns, with fiscal multipliers in advanced economies existing typically in the region of between zero to 0.5, and made assumptions consistent with this evidence (WEO, 2008).

Part of this literature however found evidence of negative multipliers. Giavazzi and Pagano (1990, 1996) for example showed that a number of fiscal adjustments were correlated with expansions in private demand in the short-term, providing evidence of "expansionary fiscal contraction". Consequently, for the management of business cycle fluctuations in particular, monetary policy was postulated as *the* central macro-economic tool.

Nevertheless, as the economic downturn unfolded, Lipsky (2008) went from suggesting in September 2008 that direct intervention should function only as a third line of defence, to, in November 2008, proposing that fiscal expansion should play a central role in managing the downturn. In doing so, Lipsky called for governments to deploy fiscal stimulus – active changes in policies that affect government expenditures, taxes and transfers – in order to support efforts taken by central banks to prevent declining economic activity, and add to aggregate demand in order to support private consumption. Similarly, Strauss-Kahn (2008d:3) noted that 'as often for the Fund, the solution to global economic problems is mostly fiscal but with a twist – it is fiscal expansion, not fiscal contraction, that we need'.

Although material events 'can be viewed in a range of fashions, legitimating varying policy responses' (Widmaier, 2005:555), calls for fiscal stimulus were not limited to the IMF but constituted part of a coordinative discourse which transcended individual beliefs of the need for intervention. This included, most notably, the newly created G20 group of state leaders which, at its November 2008 Washington Summit urged countries to take 'vigorous efforts and take whatever further actions are necessary to stabilise the financial system', while 'using fiscal measures to stimulate domestic demand to rapid effect' (G20, 2008a:2).

Although the US had already enacted a fiscal stimulus package of its own in early 2008 in the form of the Economic Stimulus Act there was an acknowledgement that to be effective fiscal stimulus would require coordination among all major countries. The London Leaders Statement for example noted that doing so would 'strengthen the impact of the exceptional policy actions announced so far' (G20, 2009:2) and should be implemented immediately.

This move seemingly constituted a significant shift in neoliberal economic ideas in the IMF which had long slighted the potential efficacy of fiscal interventions in favour of monetary policy. In this instance however, the IMF, in calling for substantial globally-coordinated fiscal stimulus, deferred to an altogether different political economy that called upon the power and resources of the state to bring about economic stability and support aggregate demand.

This was acknowledged in a speech by Strauss-Kahn (2009a:5) who noted that IMF advocacy of fiscal stimulus appeared contradictory as it was 'a novelty coming from an institution associated with belt-tightening'. Indeed, Strauss-Kahn (2010d:3) retrospectively observed that 'everyone was surprised to see the IMF, previously so liberal, become "Keynesian"'.

In doing so however, in referencing the experience of the 1930s, Strauss-Kahn (2008a:1) noted that it was important to learn the lessons of history and not react in a piecemeal way, hamstrung by old-fashioned orthodoxies, and instead suggested that it was important to act imaginatively, and be prepared to break with precedence and try new approaches.

As a means by which to justify, and persuade member states of the efficacy of, deploying substantial fiscal stimulus however, the analogy between unfolding events and the Great Depression was frequently invoked in order to convey the potential for a downturn of similar severity in the absence of exceptional policy measures (Strauss-Kahn, 2008a; 2009b; Spilimbergo et al, 2008). In doing so, speeches were 'dominated by historical analogies, whereby a sense of how bad things have been', and could be, arose 'from comparing the situation directly to other notable moments of financial meltdown' (Brassett et al, 2010:1).

Constructivist approaches are crucial in drawing our attention to the fact that the moment of failure can support a multitude of competing narratives of what went wrong and thereby what to do. Indeed it is because 'agents do not monotonically decode the material world around them and act uniformally' (Blyth, 2007:774) that states' interests are considered indeterminate as they are unsure of what course of action is in fact in their interests. As a result, persuasive practices typically come to fore, offering convincing interpretations of what went wrong, along with suggestions of what to do in the form of policy prescriptions.

Nevertheless, we can see how in this instance an inter-subjectively held consensus in and beyond the IMF developed of the need to reorient policies away from neoliberal orthodoxy. That is, at this juncture actors collectively concurred that decisive intervention could, indeed should, be made to rid the system of its accumulated pathologies (Hay, 1999:317-324).

The role of research in underpinning the shift to fiscal interventions

Notwithstanding this ostensible shift, it is insufficient from a constructivist perspective to simply state that as seemingly bad economic ideas failed others automatically took their place. To do so would provide us with little "value added" over and above a rational choice approach which shows how, during times of crises, actors move from one equilibrium to another based on a set of pre-determined exogenous interests. Therefore, what is required is a greater understanding of the means by which the IMF sought to persuade member states of the benefits of significant coordinated stimulative fiscal actions, particularly given that its effects had been postulated as minimal, even inefficacious, prior to the downturn.

With this in mind it is demonstrated how the advocacy of policies closely resembling those associated with Keynesianism was informed by a plethora of new research in the IMF, and particularly the Fiscal Affairs Department, which provided the cognitive justification for this apparent gestalt flip. This showed how at the present juncture: the concern over implementation lags was unnecessary; fiscal multipliers were higher than usual; and given its financial nature, fiscal policy would actually shorten the economic downturn.

Firstly, eschewing conventional thinking it was suggested that the decline in private sector demand would be prolonged, lasting for several quarters, something typical for downturns emanating from the financial sector (Baldacci & Gupta, 2009). Similarly, Leigh and Stehn (2009:1) showed that while responding less quickly than monetary policy, 'discretionary fiscal policy is more timely than conventional wisdom would suggest', particularly in "Anglo-Saxon" countries, the source of the downturn. Therefore, Blanchard and Cottarelli (2008:3-4) suggested that fiscal stimulus could rely more than was usual on state financed spending.

Secondly, Ban (2014:12) suggests that research by Spilimbergo et al (2008) represented 'the defining moment in the balance of epistemic power' as it 'spurned as irrelevant' existing orthodoxy. It was here that Spilimbergo et al (2008:4-5) argued the downturn, exemplified by macroeconomic conditions not experienced in decades, meant existing estimates of fiscal multipliers (the ratio of a change in output to an exogenous change in the fiscal deficit) were less reliable in informing which measures would be effective. This provided a strong argument for not relying exclusively on monetary policy (Blanchard and Leigh, 2013:19-20).

In explaining why, Almunia et al (2010), and Cohen et al (2012) suggested that, firstly, during the downturn, central banks in advanced economies cut policy rates to close to zero, a constraint which inadvertently increased the size of fiscal multipliers. Secondly a key feature of the downturn was the reduced availability of credit. This implied consumption and investment depended more strongly on current than on future income and that fiscal multipliers would be larger than typically assumed (IMF, 2013b:19; Corsetti et al, 2012).

Thirdly, research had assumed the impact of fiscal policy to be similar across different states of the economy, but new studies suggested that multipliers may be larger during periods of slack. Importantly since results were based on pre-crisis data, findings reflected mechanisms distinct from the ZLB and financial sector weaknesses. Instead, the authors appealed to the Keynesian notion that, during downturns, fiscal policy is less likely to crowd out private spending. Aurbach and Gorodnichenko (2012) for example, found that multipliers related to government spending fluctuate across the business cycle: from 0-0.5

during expansions to 1-1.5 during recessions, which suggested the efficacy of fiscal policy for the current downturn.

Finally although research pointed to the potential for “expansionary fiscal consolidations”, Perotti (2011) suggested that these findings were sensitive to how fiscal consolidation was defined, and that the most famous episodes observed in Europe in the 1980s/1990s were driven by external demand more than by internal private demand on the back of confidence effects. In the current downturn however, an IMF Policy Paper (2013b:20-21) noted that confidence effects had not played a major role so a key channel through which expansionary effects could occur – by decreasing risk premia on sovereign bonds and on domestic lending rates – was not at work since risk premia were already low in advanced economies.

This research highlights how the kinds of knowledge claims made by the IMF prior to the downturn were particular to time and space, providing persuasive arguments and calling for a particular course of policy action. Indeed, despite becoming embedded within institutional and cultural contexts, sometimes so much so that they came to be viewed as “common sense” in the IMF, neoliberal economic ideas, and the knowledge claims with which they were associated, were shown to be contingent, incomplete and subject to refutation.

This had profound effects for economic ideas which rested on a simplified understanding of monetary policy that was largely antithetical to the efficacy of fiscal stimulus. Indeed, Clift (2013:3) observed ‘the potential for an eventual recalibration of post-crisis economic policy following the dissemination of the Fund’s surprising and important research findings’.

Under such circumstances, a constructivist approach draws our attention to the fact that the kinds of assumptions made regarding the appropriate role for monetary and fiscal policy made prior to the downturn, were meaningful practices created and re-created through contingent actions which were informed by a particular set of neoliberal economic ideas.

It is here that the distinction made by Searle (1995) between ‘brute facts’ which exist independently of our conception of them; and ‘social facts’, of which ‘institutional facts’ (assumptions made in an institutional context) are a sub-set, offers a particularly useful interjection. That is, the preceding discussion shows how ‘facts’ regarding the efficacy of monetary policy was shown to have rested in a temporally-bound institutional context.

Once this is accepted it becomes evident the 'common sense' assumptions surrounding monetary policy that prevailed in the IMF prior to the downturn be considered 'ubiquitous aspects of social coordination' (Bevir & Trentmann, 2002:21). Inasmuch as this is true a constructivist approach highlights the diversity of the possible forms of economic ideas underpinning IMF policy priorities. Indeed, rejecting the assumption that there is one best way to respond to financial and economic failure seemingly opened up the potential for an alternative range of policy interventions considered off the table prior to the downturn.

Implications for the policy realm

Had new knowledge remained within the IMF its effects would have been limited. This draws attention not just to the importance of the development of ideas, but their communication through the communicative discourse. Indeed, research produced by the IMF, having major implications for the way in which the benefits of fiscal stimulus were now perceived, was deployed in such a manner as to open a window of opportunity for the enactment of policies that had been inconceivable only months prior to the downturn. This is consistent with the constructivist notion that policy ideas are those which change rapidly 'when windows of opportunity open in the face of events as old policies no longer solve the problems or fit the policies for which they were designed' (Schmidt, 2011:5).

Against this backdrop, in a speech to the Board of Governors of the IMF and World Bank, Strauss-Kahn (2008a:3) noted the need 'to deploy all of the instruments of modern macro-economic policy to limit the damage to the real economy', most notably, through fiscal stimulus. While exact measures would be guided by domestic political economy constraints, a number of principles were highlighted that should guide the scope/design of measures.

Spilimbergo et al (2008:3) for example called for fiscal stimulus that was timely (reflecting the urgency of action); large (due to the large drop in demand); lasting (due to it being a potentially long downturn); diversified (due to uncertainty as to which measures would work); collective (undertaken by all countries with sufficient fiscal space); and sustainable (to avoid long-run debt increases). The challenge therefore, was to balance the seemingly contradictory goals of large and lasting fiscal commitments, with fiscal sustainability.

These guiding principles were derived from lessons from history, or more accurately, what IMF staff thought the lessons from history had taught them, and drew on previous crises in

Korea (1997), Japan (1990s), the Nordic countries (1990s), and the US Savings and Loan crisis (1980s). From these it was deduced that, firstly, successful resolution of financial crises was necessary for growth as delayed interventions worsened macroeconomic conditions. Secondly, the solution to financial crises precedes the solution to the macro-economic crisis. Thirdly, fiscal stimulus is necessary when financial crises spill-over to the corporate and household sectors, resulting in worsening balance sheets. Lastly, the fiscal response has a larger effect on aggregate demand if it is particular to each case (Spilimbergo et al, 2008).

Against this backdrop, and translating new research into concrete, implementable policies, Spilimbergo et al (2008:4-7) advocated the following. Firstly, that public spending on goods and services has larger multiplier effects and, most important in the current context, its first round effects were more certain than those related to transfers or tax cuts. Governments were therefore advised to ensure existing programmes were not cut for a lack of resources.

Secondly, the authors suggested that spending programmes, from repair and maintenance, to investment projects should be (re)started as quickly as possible. High profile programmes with good long-run justification and strong externalities were advised both directly and through expectations. Moreover, it was suggested that the state could take a larger share in public-private partnerships for valuable projects that would otherwise be postponed.

Thirdly, three factors: decreases in wealth; tighter credit constraints; and uncertainty, were shown to adversely affect the marginal propensity to consume. Two recommendations were therefore made how to increase this propensity. The first was to target tax cuts or transfers to consumers most credit constrained such as through increased unemployment benefits, increases in earned income tax credits, and an expansion in safety nets where they are limited. The second was that clarity of policy together with a strong commitment to take whatever action may be needed to avoid the risk of a depression would reduce uncertainty, and lead consumers to decrease precautionary saving and stop waiting and start spending.

Finally it was suggested that just as consumers were operating in an uncertain environment, so too were firms taking a wait-and-see approach to their investments. The challenge for policymakers, it was therefore suggested, was to avoid a situation in which firms cut back their operations for lack of reasonably-priced credit. Although traditionally the concern of monetary policy, the authors pointed towards scope for governments to support firms by combining procedures that allow the restructuring of firms facing economic distress with government guarantees on new credit. This, so the argument proceeded, could be made on the implementation of a restructuring plan, an approach underlying IMF-supported programmes: lending plus policy adjustment (see also Blanchard & Cottarelli, 2008).

Implications for the neoliberal economic philosophy

The foregoing discussion is consistent with constructivist research which suggests that policies are the areas that change most rapidly in the context of crises as the cognitive ideas underpinning their justificatory and persuasive practices are shown to be unable to deal with the problems facing policymakers (Schmidt, 2011:2). Economic philosophies however are typically confined to the normative, as opposed to the cognitive, sphere, a reflection of ideas regarding the appropriate role of states or markets. That these ideas are inherently political means that they are typically those which prove most resistant to change.

Nevertheless, the policies advocated by the IMF during the second phase of the downturn, and the ostensible break with orthodoxy with which they were associated, also appeared to have important implications for the neoliberal economic philosophy. Therefore, although often slow to change, chapter two demonstrated that significant change does and can occur, and the unfolding downturn appeared to present such a potential.

That is, prior to the downturn, and during its first phase, there was an assumption within the IMF that fiscal policy should be limited to minimizing distortions and letting automatic stabilizers work. Nevertheless, that monetary policy failed both to prevent banking and financial sector pathologies from impacting severely on the real economy and thereafter to sufficiently redress the downturn, led Romer (2011:1) to note at an IMF conference in 2011 that the downturn had 'shattered some of the core tenets of macroeconomic policymaking'.

Indeed, in a 2009 Commentary Stiglitz (2009:1) appeared to reflect something of a consensus of the time, suggesting that 'we are all Keynesians now'. Freedman et al (2009:6) of the IMFs Research Department for example noted that interest in Keynesian economic ideas was even common among those who had outright rejected its potential efficacy.

What was happening was, according to Stiglitz, the triumph of reason and evidence over ideas and interests, most notably, a particular set of neoliberal economic ideas that had privileged the market and the de-politicization of key policy instruments. Indeed, Stiglitz noted that for those Keynesians who had been marginalised and shunned for more than three decades, the return to Keynesian economic ideas represented a moment of triumph.

Chapter 2, which observed a shift from Keynesian to neoliberal economic ideas, draws our attention to the fact that the potential for such a shift is not without historical precedence. Indeed, Bevir and Trentmann (2002:1) note how history is characterised by two forms of economic coordination which have been valorised by policymakers, the market (a natural and spontaneous order), and state intervention (where states took control of the economy).

Although the efficacy of the market had long been the dominant assumption in the IMF, calls for significant fiscal interventions seemingly imposed a new trajectory on the state as problem definitions and policy priorities again came down on the side of privileging state intervention (Hay, 1999:317). Indeed, that responsibility was once again placed on the shoulders of governments to intervene to prevent the most severe effects of the downturn suggested the repercussions of this shift could be pivotal given that economic philosophies are 'generally portrayed as most long lasting' (Schmidt, 2011:5; Schmidt, 2008, 2010, 2012).

This characterisation of the downturn and its potential implications for the neoliberal economic philosophy highlighted the temporally bound nature of neoliberal economic ideas, even those so deeply held that they resided largely un-questioned in the background, yet whose realities had the potential to be transformed as prior assumptions were discredited by economic turbulence. This draws attention to the contingency of the socially constructed nature of the economic ideas steering global economic governance which were shown as being but one socially constructed economic order out of a number of possibilities available.

This was consistent with constructivist approaches that have sought to correct for the re-productive logic of much rational choice IPE (Chwieroth, 2010; Widmaier et al, 2007). The result is an analysis of the failure of monetary policy and shift to support for fiscal interventions as an ostensible crisis of a policy area inherent to neoliberal economic ideas, in which it was recognised that a decisive intervention must be made.

It is here that the second phase of the downturn was seized upon as a potential ‘epoch-making’ moment delineating between phases of political-economic times, a deviation from the normal course of events (Hay, 1999:317). Indeed, Broome et al (2012:7) noted that efforts were immediately made ‘to paint the present juncture as an epoch-shaping moment: the dawn of “post-neoliberalism”, or even the arrival of “post-capitalism”’, according to which narratives ‘the GFC should be read as a signal event, a watershed moment’.

There therefore appeared to have been a major shift from the de-politicisation of policy instruments acting in pursuit of a single policy goal, to a more active role for the state in managing the economy. In this regard, the second phase of the downturn seemingly provided all the pre-conditions necessary for a widely-interpreted moment of crisis in which economic orthodoxy in the IMF would be subject to a significant transformation.

Concluding remarks

This chapter has sought to substantiate two claims. Firstly, that during its first phase, the IMF interpretation of the downturn was one emanating from the sub-prime mortgage market and a broader liquidity event as banks became unwilling or unable to lend to one another, ultimately precipitating a slow-down in real economic activity. In response the IMF advocated that monetary policy operate as the first line of defence in the form of interest rate easing, and latterly, two rounds of UMPs. These policies however, despite their increasingly unconventional nature, continued to be derived from the intellectual frames provided by the prevailing neoliberal economic philosophy and problem definitions.

Secondly, as 2008 progressed it became increasingly evident that monetary policy and central bank interventions alone would be unable to prevent the transmission of the downturn from the banking and financial sectors to the broader economy (the second phase). In response, the IMF advocated that governments with sufficient scope to do so provide significant fiscal stimulus in order to stimulate aggregate demand in such a manner that would support private consumption to prevent further declines in economic activity.

It is this ostensible shift in economic ideas within the IMF that has been seized upon to suggest the existence of a potentially epoch-shaping shift in neoliberal economic ideas. Indeed, IMF Managing Director Christine Lagarde (2013:2) observed the potential for such a shift, suggesting that 'the pride of this institution is to constantly question, challenge, revisit, re-examine, and test its findings and assumptions, in order to be as up-to-date as possible'.

Nevertheless, Chapter 5 suggests that even if moments of political-economic failure demonstrate that dominant ideas and knowledge assumptions are flawed, change need not be the natural corollary. Indeed, a key assumption of this research is that upon entering its third phase (a focus on sovereign debt sustainability) the IMF sought to frame the downturn in such a manner that divergence from the prevailing neoliberal economic philosophy, problem definitions and policy interventions was postulated as neither desirable nor effectual.

Chapter 5

Economic Policy II

'If it were done when t'is done, then 'twere well it were done quickly'
(Macbeth)

Introduction

The previous chapter charted the IMF policy response during the first two phases of the downturn. In doing so it was demonstrated how, despite being considered resolvable with policies consistent with neoliberal economic ideas during its initial phase, the infiltration of banking and financial sector pathologies into the broader economy (the second phase) led the IMF to advocate a series of unorthodox policy interventions. Indeed it was assumed that, having 'shaken the foundation of our economic framework' (Lagarde, 2012a:4), the ostensible crisis had brought with it a potentially major shift in economic ideas in the IMF.

Nevertheless, this chapter substantiates two key claims. Firstly that although there has been some change in the IMF regarding the perceived worth of a range of policies deemed largely ineffectual prior to the downturn (fiscal policy for example), as it entered its third stage in late 2009/early 2010 (a focus on sovereign debt sustainability) it became increasingly evident that the IMF had maintained a normative commitment to the neoliberal economic philosophy and the manner in which economic problems were framed and responded to.

Secondly, this chapter demonstrates how the IMF has in fact sought to frame the third phase in such a manner that the further entrenching, as opposed to retreat from, policies consistent with neoliberal economic ideas are desirable from a normative perspective and necessary from a cognitive perspective. Therefore, although the downturn certainly provided a permissive context in which to effect a major transformation in economic ideas in the IMF, change need not be, indeed nor has it been the natural corollary.

Phase 3: Problem definition

As of late 2009 the second phase of the downturn (the most acute phase) appeared to be over. Economic growth appeared, albeit minimal and uneven, to be recovering and acute risks to the financial sector had subsided. Against this backdrop, the attention of the IMF shifted towards ‘a new kind of problem’ (Strauss-Kahn, 2011a:2) sovereign debt, which had increased substantially during the previous two phases as a result of major support to the financial system and declining tax receipts brought about by the accompanying recession.

Given the range of problems facing policymakers however, there was nothing inherent to increasing sovereign debt that meant it ought to be perceived as the predominant problem. Indeed, this chapter draws attention to the importance of framing in the IMF, that is, in terms of the diagnostic function it performed (highlighting excessive sovereign debt) and also the prognostic role in terms of the kinds of policies the IMF considered necessary to address the problem so defined (those consistent with neoliberal economic ideas).

That it sought to affect interpretations of the problem by assigning meaning to increasing sovereign debt burdens suggests that IMF actions at this juncture be best considered part of a constructivist strategy (Benford, 1997:410; Oliver & Johnston, 2000:8). In doing so framing emphasises the intentional ways in which the IMF sought to construct representations to draw support from others. That it did so points to critical processes of social construction (Oliver & Johnston, 2000:1) and highlights that the material 'reality' presented by increasing sovereign debt was not a self-apparent phenomena that dictated an obvious response, but was identified, collated and packaged by the IMF in order to highlight a particular issue as being more salient than others at that moment in time (Benford & Snow, 2000:623).

We therefore show how 'meanings do not automatically or naturally attach themselves to the objects, events, or experiences we encounter, but often arise, instead, through inter-actively based interpretive processes' (Snow, 2004:384). Indeed, by framing the third phase in such a manner, by highlighting what was relevant over other problems that may have been equally, if not more salient, the parameters for what was going on were set and appropriate policy responses were limited from the outset. This highlights how framing was deployed by the IMF in such a manner as to act as a key dynamic for collective action.

This draws our attention to the discursive power of the IMF in terms of its ability to confer meaning on to events. That is, a primary determinant in the fixing of an objects meaning is the power to evacuate the meaning of what it is not. Acknowledging this point foregrounds both the agency and power relationships which were exercised by the IMF in such a manner as to fore-close all other meanings, in this case what seemingly excessive sovereign debt burdens meant to member states. Doing so helped to set the terms for the broader debate by foreclosing the possibility of any serious deliberative argument taking place, and essentially, negating the need for such argument to take place at all (Epstein, 2008:9-10).

In this particular instance, Baldacci et al (2010) drew attention to soaring sovereign debt burdens which were projected to rise in the G-20 advanced economies from 73 percent of GDP at end-2007 to about 108 percent of GDP at end-2015, the largest rate since World War 2. This underscored a shift in narrative in the IMF (for our purposes, the third phase) from one of support for fiscal stimulus to the need for fiscal sustainability which, in a 2009 speech, Lagarde (2009:2) noted was one of the major challenges facing the global economy.

Similarly the Fiscal Monitor (2010:5) suggested that 'without progress in addressing fiscal sustainability concerns, high levels of public debt could weigh on economic growth for years', as even that insufficient to result in overt debt crises had the potential to become a burden on long-term growth. Indeed, Lagarde (2012:2) noted that high public debt was already acting as 'a drag on the already-low growth prospects in advanced economies'.

Interpreting the potential implications of excessive sovereign debt and drawing attention to the need for intervention in the manner that it did essentially constituted an attempt by the IMF, to draw back from exceptional fiscal support advocated during the second phase of the downturn. Moreover however, this was accompanied by the suggestion, consistent with assumptions made prior to the downturn that fiscal policy should be limited to letting automatic stabilizers work, and provide a stable macroeconomic framework for growth.

Nevertheless, given the severity of the downturn, declining investment and consumption, stagnant or declining incomes, soaring unemployment, and the potential for their worsening should fiscal retrenchment be undertaken unnecessarily prematurely, it was crucial that the IMF persuade states that undertaking this endeavour was consistent with their interests.

Here, the IMF played a critical role in providing a convincing narrative of unfolding events. This included more than simply engaging in providing road maps that defined the most appropriate route by which to successfully navigate from A to B. Rather, the persuasive practices undertaken by the IMF actually sought to posit that going from point A (excessive sovereign debt burdens) to point B (fiscal sustainability) was a good idea and consistent with the interests of member states (Blyth, 2007:762; Schmidt, 2011). That the IMF embarked on such an endeavour draws our attention to the power of persuasion, through the provision of research, as a crucial mechanism of social construction.

In doing so the IMF provided cognitive justification in the form a sustainable debt threshold, beyond which growth would be adversely affected. This served to reify the perception of the problem of excessive sovereign debt as a situation in which intervention ought to be made. Indeed, Strauss-Kahn suggested in a 2011 speech (2011a:2) that research would play an important part in guiding policymakers and it was here Cottarelli (2012:2) noted the need for action was provided by ‘a consistent body of literature that finds significant effects of high public debt on potential growth’ its self considered essential for fiscal sustainability.

Kumar and Woo (2010:3) of the IMF’s FAD for example postulated the existence of an inverse relationship between initial debt and subsequent growth: on average, a 10 percent increase in initial debt-to-GDP was associated with a slowdown in real per capita GDP growth of around 0.2 percent each year, with the impact being marginally smaller in advanced economies (around 0.15 percent). Moreover, the authors found evidence of non-linearity, with levels of debt exceeding 90 percent of GDP having negative effects on growth.

These findings were broadly consistent with Carmen Reinhart and former IMF chief economist Kenneth Rogoff (2010:2) who similarly found that the link between growth and debt is relatively weak when debt resides at normal levels, yet median growth for countries with public debt over 90 percent of GDP are roughly 1 percent lower than would otherwise be the case, and with average (mean) growth rates as much as several percent lower.

Attempts to quantify the dangers associated with excessive sovereign debt burdens were crucial for the IMF. That is, because analysis was based on simple numbers and a seemingly straightforward debt threshold above which economic growth would be compromised, an attempt was made to portray them, and their effects as impartial. This provided a defence against accusations of politicization that might undermine credibility, rather, their seemingly objective nature allowed for garnering political support (Barnett & Finnemore, 2004:69).

This approach was therefore crucial because for frames to become naturalized, that is to say, for them to become part of the natural order of things, they must gain legitimacy and invoke some semblance of trust. They do so by being grounded in cognitive justification which makes their potential for becoming established all the more viable (Adler, 1997:340).

This research had two important implications. Firstly, Strauss-Kahn (2009b:2) noted that 'building up fiscal space in good times is very important to allow sufficient space for fiscal stimulus in crisis times'. Indeed, Blanchard et al (2010:14) suggested that had governments been better placed to adopt a more expansionary fiscal stance, they would have been better placed to fight the downturn. That is, in countries with high pre-crisis ratios of public sector debt-to-GDP, lack of fiscal space both constrained the ability to implement timely counter-cyclical policies, and undermined the effectiveness and the quality of fiscal performance.

Secondly, research pointed to the need to reduce fiscal debts and deficits from their current levels. Cottarelli (2009:2) for example questioned whether stabilising debt at its post-crisis level was enough, as, 'if a debt ratio not exceeding 60 percent – as noted, the pre-crisis median level – was regarded by many countries as an appropriate norm before the crisis, it should continue to appear so after the crisis' (see also Fiscal Monitor, 2010:3).

The problem however, according to Cottarelli (2012), was that since the 1970s, although public debt in advanced economies had acted as the ultimate absorber of crises during the bad times, this was seldom accompanied by reductions in the good times. This was a key distortion of the deficit bias; budgets rarely alternated between periods of surplus and deficit, but rather remained in deficit. Indeed, Baldacci et al (2009:3) noted that only 12 percent of countries suffering crises had reduced debt to pre-crisis levels after 16 years.

Cottarelli (2012) therefore suggested that debt levels, not reached before without a major war, should not be allowed to follow a similar path. This reflected a growing consensus within the IMF and beyond that this time things should be different, and the ultimate goal should be a reduction of public debt ratios over time (see also Strauss-Kahn, 2011).

These assumptions appeared all the more pertinent given the unravelling sovereign debt positions in the euro area which had demonstrated that while a weak fiscal position was not a sufficient condition to be under market pressure, it was a necessary condition. Indeed it was against this backdrop, Strauss-Khan (2010:2) noted that ‘all countries – especially advanced economies with a high level of debt – have to go back to fiscal sustainability’.

To be sure, that fiscal adjustment was not advocated in the total absence of a recognised need for some degree of flexibility, has led to some confusion and debate as to the extent to which fiscal policy ideas in the IMF are indeed characterised by change or continuity. This demonstrates how the IMF did not present the need for adjustment as a ‘one-size-fits-all’ approach, but to paraphrase Lagarde (2011a:2) ‘a moment of choice’ with each state having the capacity to identify the speed and context in which adjustment takes place.

On the one hand it was recognised that, for some, a retreat to austerity (a period of living within diminished means) would, be simply deleterious. The G20 Toronto Declaration for example observed that ‘there is a risk that synchronised fiscal adjustment across several major economies could adversely impact the recovery’ (G20, 2010:3). This assumption was supported by the IMF, with Strauss-Kahn (2009c:3) cautioning that 'policymakers may jeopardise the recovery by exiting from crisis measures too soon’ and in doing so, mitigated a key concern of critics of adjustment: that it suffers from a ‘paradox of thrift’ (Jabko, 2013:706) that if all states tighten their belts simultaneously demand plummets.

Superficially at least, this contradicted the assertion made by the IMF that frontloaded consolidations were the most effective approach to restoring the health of public finances. This was derived from research suggesting that it would: maximise debt reduction; minimise uncertainty about future consolidation needs; and boost long-term growth (IMF, 2013b).

Nevertheless, a view emerged within the IMF that excessive frontloading might undermine social cohesion, weaken market confidence, and ultimately prove self-defeating. Indeed, in a 2012 speech, Lagarde (2012b:3) stated that IMF research 'finds that fiscal multipliers are quite large in downturns, meaning that an overly-aggressive adjustment today will hurt growth, and might actually also raise public debt ratios’. We might not therefore be without justification in following the Ban and Gallagher (2015:137) who note that ‘these changes should not be downplayed’ as these “edits” were in fact quite extensive when compared to assumptions made prior to the downturn (see also Ban, 2014).

On the other hand however it is suggested that these concessions notwithstanding, the IMF continues to defer to the existing neoliberal economic philosophy and problem definitions. That is, while acknowledging frontloaded consolidations may be self-defeating, the IMF has however suggested that excessive delay could be even more costly if confidence was lost in governments delaying adjustment, thereby leading to higher interest rates, an inability to service debt, and declining output. Therefore, although there were instances where the IMF noted cutting deficits was not an immediate priority, even here 'programmes were lengthened and targets adjusted, but the underlying logic was the same' (Blyth, 2013a:738).

Indeed, at his opening address to the 2010 annual meeting of the Board of Governors of the IMF and World Bank, Strauss-Kahn (2010:2-3) appeared to offer unequivocal clarification of the IMF's position in stating that 'I sometimes read in the newspaper that the message from the IMF is a bit blurred, not that clear; that the IMF doesn't know exactly if it's pushing for growth or pushing for fiscal retrenchment. *Our message is clear and consistent. In the medium term, there is a need for fiscal sustainability. Everything has to be done to go in this direction in the short term'* (emphasis added; see also Lagarde, 2011a:3; Lipsky, 2011:2).

In order to persuade member states of the need to do so, the IMF consistently referenced the context provided by excessive sovereign debt burdens as being analogous to the post World War Two context, the last time average sovereign debt was as high (Cottarelli, 2012; Cottarelli& Jaramillo, 2012; Lipsky, 2011). Notwithstanding the fact that existing debt levels were lower, Cottarelli (2013b:2) noted the situation facing policymakers was more grave as: most of the fiscal adjustments then consisted of cuts in military spending; current spending on pensions and health-care is rising; long-term growth prospects are lower; and financial repression in the 1950s facilitated the financing of public debt, restrictions not now in place.

The preceding discussion shows how the potential for alternative models of policy reform were largely screened out by the IMF which identified the nature of the problem (excessive sovereign debt), along with the appropriate solution (fiscal adjustment). Despite a number of economic ideas regarding the relative efficacy of monetary and fiscal policy seemingly being destabilised, cognitively speaking, by the downturn, upon entering its third stage it became increasingly evident that the IMF continued to exhibit a cognitive and normative commitment to the neoliberal economic philosophy which again was the frame through which political-economic problems were interpreted (the need for fiscal sustainability).

That these assumptions once again assumed prominence within the IMF as sovereign debt positions worsened may not in themselves appear to be overtly problematic, particularly given their cognitive underpinnings. However, it was for two key reasons.

Firstly, one of the most cited examples of the implications of the negative effects of government debt beyond a particular debt-to-GDP threshold on economic growth was that by Reinhart and Rogoff (2010). However, this research has been shown to be replete with data anomalies, absences, and errors which provided a wholly inaccurate representation of the relationship between public debt and GDP growth rates (Herndon et al, 2013:1).

Secondly, empirical evidence seemingly contradicted the research and pointed to the fact that there existed in reality a number of variables impacting on sovereign debt and growth. Blyth (2013) for example suggests that the GDP growth of Japan had been good in the run-up to the downturn, despite having a debt-to-GDP ratio in excess of 150 percent. Moreover, that of Italy had been 105.7 percent in 2002 but was not interpreted as being problematic, yet by 2009, although at the same level, was suddenly perceived as being a major problem requiring major policy interventions to place back on a sustainable footing.

What changed in the intervening period therefore were not debt levels, but the manner in which they were now framed, and therefore, the perceptions of what the IMF thought this now meant. This shows how, rather than 'facts' being endowed with a particular meaning to which agents respond, the shifting problem definition meant data was 'redefined and linked to new stories and narratives where the same numbers now mean something completely different' (Kessler, 2012:282). Indeed, that data does not come with an information particle that flows from actor to actor, draws attention both to the power of interpretive processes, and the assumption that "problems" are not simply "out there", they are what we make them to be, that is, 'problems exist because we talk them into existence' (Cohn, 2013:114).

This demonstrates how, despite having seen sovereign debt increase substantially as a result of both financial sector bailouts and falling tax revenues brought about by the accompanying downturn, along with research demonstrating that excessive sovereign debt burdens were shown to adversely affect economic growth 'a crisis of finance was deftly constructed as a crisis of the profligate state' (Blyth, 2013:210; Gamble, 2014).

In lieu of this interpretation of the prevailing problem, an attempt was made by the IMF to influence the broader debate in which policymakers perceived their interests by providing cognitive justification for its continuing normative commitment to the neoliberal economic philosophy. The aim of doing so was to limit policy options facing policymakers by positing the need to return to fiscal solvency and sustainability.

It was here again that, just as knowledge-based experts within the IMF had been at the forefront of providing the cognitive justification for unorthodox policy interventions during the second phase of the downturn, so, paradoxically, were they now engaged in providing contrasting narratives of the third phase. In doing so, calls centred on the need – in light of the research highlighting the negative implications of excessive sovereign debt burdens - for a return to emphasising prior assumptions regarding the appropriate role for fiscal policy.

This narrative, imbued with the discourse of the neoliberal economic philosophy, therefore attempted to ensure that the frames in which fiscal policy problems were defined and responded to prior to the downturn did not disappear. On the one hand, the IMF continued to advocate prudent fiscal policy in the form of low budget deficits and low public debts which were again considered key for economic growth and poverty reduction (IMF, 2005).

On the other hand, calls for increased fiscal space were consistent with prior assumptions that it was necessary for country's to build up reserves in good times so that they could be drawn on during bad times. The IMF (2006; 2013b) therefore suggested that unlike highly indebted sovereigns, countries with low levels of debt would be able to increase their fiscal deficits through borrowing in such a manner that they would not lose market confidence. Indeed, it was observed that in the absence of such buffers, countries were often forced to take emergency fiscal measures that further damaged growth and social indicators.

Implications for the neoliberal economic philosophy

The rapid shift between advocating fiscal stimulus during the second phase of the downturn and then back towards neoliberal orthodoxy during its third phase rejects the assumption that it might prove to be a re-constitutive event for the IMF. Although this was ultimately not the case, the preceding discussion did observe something of a paradox. That is, the same knowledge-based experts who called for, and provided cognitive justification for, the deployment of fiscal stimulus were the ones who helped precipitate a call for a retreat to orthodoxy during the third phase of the downturn through calls for fiscal adjustment.

In accounting for why this is so, this research makes a simple assumption. The IMF, and, most notably, the G20, never abandoned their normative commitment to the neoliberal economic philosophy. As a result, the policies undertaken during the second phase can be more aptly understood as being more concerned with failure management, a means to protect the system from its follies rather than change it to any significant degree.

This helps us to understand why economic problems were framed in the manner they were during the third phase, that is, they were derived, embedded in, and bounded by, aspects of the broader neoliberal discourse which shows how the framing process undertaken during the third phase was bound by existing economic orthodoxy (Snow, 2004:385).

Indeed, as the second phase of the downturn unfolded, policymakers were faced with a moment of severe danger during which, to prevent a more serious catastrophe, all policy levers were pulled regardless of how conventional or otherwise they might have been. Of fiscal stimulus for example, Blyth (2013:209) noted that although the IMF had championed belt-tightening for developing countries, it eschewed orthodoxy and 'turned on the money pumps for the developed world at the first hint of trouble'. Similarly, Gamble (2014:62) suggested that in contrast to developing economies 'the advice changed and the IMF endorsed radical emergency measures to stabilize the financial system and to provide extensive and unconditional fiscal and monetary stimulus to keep the economy afloat'.

This suggests that little time or thought was given to what the longer-term implications of policy actions might have been. There was certainly no intention to reconsider the efficacy of the neoliberal economic ideas that had driven global economic governance during the preceding decades. To suggest that the policies advocated during the second phase could be construed as anything other than an attempt to save neoliberal economic ideas from their follies would therefore be to misread the intentions of the IMF at that time (Gamble, 2014).

Although Lagarde (2009:4) described the IMF as 'an intellectual leader during the crisis' on account of its early call for fiscal stimulus, the advocacy of the deployment of fiscal interventions was evidently not the result of a deliberatively articulated ideational shift, nor was it a response to an ostensible progressive accumulation of pathologies in neoliberal economic ideas as had been the case in the move away from Keynesian economic ides.

It has been suggested that knowledge-based experts play a vital role in clearing the ground for alternative problem definitions and policies that might better address pressing problems (Schmidt, 2011). In this instance, this was clearly not the case as research highlighting the beneficial impact of fiscal stimulus followed only in late 2008 long after Strauss-Kahn had initially called for its deployment for states that were ably positioned to do so in early 2008.

That the IMF continues to privilege prior assumptions regarding what it sees as the correct role for fiscal policy therefore suggests that, 'despite having recently raised expectations about reforms in its fundamental policy stance, the IMF remains a long way from jettisoning the neoliberal principles of its governing macro-economic framework' (McKinley, 2010:3).

Rather, the IMF continues to exhibit a considerable degree of stasis in the kinds of problem definitions it projects, which are themselves derived from the neoliberal economic philosophy that existed prior to the downturn. As a result, there has been no significant transformation in the manner in which new circumstances are framed and responded to.

Therefore, despite the severity of the banking and economic downturn, the advocacy of the deployment of fiscal stimulus, and research pointing towards the efficacy of fiscal policy under certain conditions, the IMF and other actors constituting the coordinative discourse continue to exhibit considerable faith in the benefits of the neoliberal economic philosophy.

In doing so, an explicit normative assumption was once again made regarding what the IMF considered an appropriate role of states and markets in the management of the economy. This was manifest in terms of support for prior assumptions regarding the efficacy of monetary policy interventions on the one hand, and minimal state interventions through a less active fiscal policy, limited to letting automatic stabilizers work, on the other hand.

This shows how the manner in which the IMF responded to the second phase of the down-turn (the most acute phase) continued to be responded to within the 'discursive fields' (Steinberg, 1998:856) which the IMF drew upon to diagnose, and provide a prognosis of, appropriate courses of action. As a result, events continued to be interpreted through existing frames of intellectual reference provided by neoliberal economic ideas.

This was observable from as early as the April 2009 London Summit, in which the Leaders Statement noted after advocating the deployment of significant discretionary fiscal stimulus only six months prior, that 'we are resolved to ensure long-term fiscal sustainability and price stability and will put in place credible exit strategies from the measures that need to be taken now to support the financial sector and restore global demand' (G20, 2009:2).

However, it was the 2010 G20 meeting in Toronto that signified the politics had changed fundamentally as the discourse shifted from the need for fiscal stimulus to sustainability, with states agreeing on 'following through on fiscal stimulus and communicating "growth friendly" fiscal consolidation plans in advanced countries that will be implemented going forward. Sound fiscal finances are essential to sustain recovery, provide flexibility to respond to new shocks, ensure the capacity to meet the challenges of aging populations, and avoid leaving future generations with a legacy of deficits and debt' (G20, 2010:2).

This, Payne (2014:4) noted, constituted 'the end of global Keynesianism' as future meetings, despite the occasional allusion to the contrary, 'did not seek to tackle the notion of 'growth friendly fiscal consolidation''. Rather, it was here that 'the neoliberal old guard… began to strike back' (Blyth, 2013:208), as not only were neoliberal economic ideas not undermined despite failings in goals and instruments, it was, in the short term, seemingly re-enforced.

Early calls for the shift away from exceptional fiscal support to planning and implementing exit strategies were similarly reflected by senior officials in the IMF. Indeed, although the second phase of the downturn had placed counter-cyclical fiscal policy back at centre stage, from the very beginning its advocacy was couched in orthodox assumptions, tempered as it was with the fact that it should be balanced against the importance of fiscal sustainability.

Lipsky (2009:2) for example noted in a 2009 speech that 'although fiscal policy should remain expansionary... it is not too early to begin planning to unwind the extraordinary policies that have been put in place'. This was a point iterated by Strauss-Kahn (2008b, 2009, 2010) who similarly observed that fiscal policy should be temporary, grounded in medium-term fiscal consolidation frameworks, and unwound at the earliest opportunity.

We can therefore observe among the institutions of the coordinative discourse a continuing normative commitment to belief in the efficacy of the neoliberal economic philosophy, problem definitions and policy priorities. These ideas were not simply the aggregation of the individual beliefs held by these institutions but were, more fundamentally, held as collective knowledge regarding the perceived efficacy of neoliberal economic ideas (Adler, 1997:327).

The consequence of this was that by calling for a retreat from exceptional fiscal support, an attempt was made by the IMF and G20 to determine the broader context for action. As part of this process the discourse coordinated by these actors sought to steer, frame and set an agenda which supported calls for fiscal adjustment to address sustainability concerns. In doing so, an attempt was made to craft a normative consensus about the appropriate role of fiscal policy, and what values should inform the operating of the global economic system.

As part of this process, debate was inherently limited, confined as it was to a small number of global economic governance institutions who held inter-subjective ideas regarding the appropriate role of fiscal and monetary policy. As a result, the policy debate was concerned not with whether or not fiscal adjustment was appropriate when unemployment was high and the recovery slow, but at what pace it should be carried out given high levels of debt.

Therefore, despite assumptions to the contrary during the second phase of the downturn, the IMF again acquiesced to prior assumptions that discretionary fiscal policy would have only a limited role to play in both the day to day running of the economy and in helping to fight recessions, with monetary policy retaining primacy as key macroeconomic policy tool.

Indeed, we can see that, further to the IMF emphasising the need for fiscal sustainability, so too has it not followed that fiscal policy might play a more important role in managing the economic cycle in the future. Rather the advocacy of fiscal policy was consistently couched in the context of the ‘exceptional circumstances’ (Blanchard, 2010:9) presented by the downturn as opposed to being considered a more significant part of the policy mix.

As a result, research showing that: fiscal policy was more efficacious than was thought; and expansionary fiscal contraction was not as convincing as was conceived, has not had a substantial impact on conventional thinking in the IMF, despite allusions to the contrary.

This suggests the seeming enlightenment regarding fiscal interventions has not translated into their becoming a more significant part of the management of the day to day running of the economy. Rather, the IMF continues to frame the appropriate form and function of the role of fiscal policy in much the same manner as it did prior to the downturn.

This was an assumption largely supported by an IMF (2013b) Policy Paper analysing the impact of the downturn on fiscal policy which similarly questioned whether it had implied a fundamental change in the way it would operate in the future. The suggestion was that 'in normal times, in normal economic fluctuations monetary policies, together with the use of automatic stabilizers will remain a key tool to control the economic cycle'(IMF, 2013b:2).

This was premised on evidence which suggested that although the down-sides to fiscal policy were not as large as envisaged, there continued to be down-sides in normal times. These included the risks of asymmetry (it is easier to expand than tighten) and the fact that there were lags in formulating and implementing fiscal measures due to awkward political processes (Blanchard, 2010:9). As a result, the IMF (2013:1) concluded 'that earlier concerns about whether discretionary fiscal stimulus measures will be timely and reversible remain valid, especially during less severe recessions'.

An assumption was therefore made that monetary policy should continue to be privileged in the day to day running of the economy and remain the first line of defence in fighting down-turns. Indeed, Blanchard (2010:10) stated that 'it is important to start by stating the obvious, namely, that the baby should not be thrown out with the bathwater. Most of the elements of the pre-crisis consensus, including the major conclusions from macroeconomic theory, still hold. Among them, the ultimate targets remain output and inflation stability'.

This echoed the point made by other senior IMF officials. Vinals (2010:1) for example noted that 'in my view, the appropriate arrangements are for monetary policy to continue to be geared to preserving price stability' which 'must remain the primary objective of monetary policy, supported by central bank independence, as well as strong accountability and clear communication'. Similarly Strauss-Kahn (2010:3-4) stated in his opening address to the 2010 meetings of the board of governors of the World Bank and IMF that, 'let me also be clear: we remain an institution that believes that low and stable inflation delivers positive benefits for growth and macro-economic stability. That remains the IMF's key message', and as a result, 'many tenets of the pre-crisis consensus – notably low inflation and fiscal discipline – remain valid' (see also Strauss-Kahn, 2011a:1).

As a result, although there were times when the IMF considered that discretionary fiscal stimulus would be important, the assumption was that those instances were limited, applicable only to 'cases in which conditions are similar to those that have prevailed in the last few years' (IMF, 2013d:2). This was a point iterated in the IMF Policy Paper (2013b:4) which noted that fiscal policy is useful when 'conditions resemble those prevailing in advanced economies in the post-crisis period'; and again by division chief of the FAD Bernardin Akitoby who suggested that 'fiscal policy can have powerful short-run effects on the economy *when economic conditions resemble those that have prevailed in many advanced economies over the last few years'* (quoted in IMF, 2013e:1, emphasis added) including when policy rates were at the ZLB and the financial sector was weak.

In deferring once again to the perceived efficacy of the neoliberal economic philosophy, problem definitions and policy priorities, we can see how the IMF sought to reassert prior neoliberal economic ideas. Indeed, Steinberg (1998:854) draws our attention to the fact that every social order has a particular set of ideas that privileges some stylizations over others, that is typified by a particular set of vocabularies, meanings, rules for using them in dialogue, and providing a lens for viewing an aspect of political-economic life.

In this instance, we can see how the IMF sought to once again stabilize the flow of meanings for communication. That is, discourse was once again characterised by such concepts as fiscal sustainability, fiscal adjustment, deficit reduction and the need for sound finances. This discourse however, was the medium through which the IMF, along with the G20, once again attempted to define the common sense of political-economic life by objectivising and naturalizing definitions of events and their meanings for states (Steinberg, 1998:854).

Doing was a clear expression of power. However, it was deployed in this instance in such a manner as to bind the range of problems to be defined. This reminds us that an essential part of power is produced through discourse, that is, the capacity to construct silences in the process of constructing common sense. This is manifest not only in attempts to assign meaning, but in the capacity to construct silences, as if states are focused on one set of problems, their attention is turned away from others which are not subject to discussion.

Together therefore an assumption is made that the inability of monetary interventions to sufficiently stem the banking and financial sector turmoil, along with the failure of monetary policy to prevent the transmission of the banking and financial collapse to the real economy, while having '*challenged* our pre-crisis views about fiscal and monetary interactions' (IMF, 2013b:13; emphasis added) have not in fact *changed* them to any significant degree.

Policy implications

The preceding discussion has suggested that the cognitive rationale upon which calls for fiscal adjustment was premised was inherently contested. Nevertheless, the remainder of this chapter shows how the sovereign debt narrative was framed by the IMF in such a manner as to advocate policies that went far beyond attempts to remedy for an economic downturn whose origins were specific to policies failures in the banking/financial sectors.

Doing so draws our attention to the importance of the prognostic role associated with framing problems in a particular manner. That is, frames are shown as being important in not only performing an interpretive function in the sense of providing diagnostic answers to the question of what is going on, but also as being inherently agential in the sense of calling for a particular course of policy action to remedy the problem so-defined (Snow, 2004:385).

Viewed in such a manner, the framing process undertaken during the third phase of the downturn played a crucial part in helping to mobilize collective action. Doing so was an attempt to stabilize and entrench adherence to the frames provided by the IMF within the broader neoliberal discourse. In this regard, framing processes are fundamental for not just drawing attention to particular events, but in mobilizing action (Benford, 1997:410). This is consistent with IMF assumptions that research 'will almost inevitably carry policy messages' (IMF, 2011:1) as it is this which gives it real relevance for policymakers.

Indeed, Lagarde (2011:3) stated in a 2011 speech that ‘before talking about solutions, we need to be clear about the problems’. Having framed the third phase (and therefore the problem) in a manner consistent with neoliberal economic orthodoxy as one of excessive sovereign debt requiring fiscal adjustment, this meant that appropriate responses were similarly derived from the policies provided for by neoliberal economic ideas (the solution).

In this particular instance, by framing and diagnosing the problem as one of a sovereign debt excesses, this served to constrain the range of '"reasonable" solutions and strategies advocated' (Benford& Snow, 2000:616), which in this case took the form of the need for, on the one hand, fiscal adjustment, and on the other, growth-enhancing structural reforms.

Indeed, Strauss-Kahn (2009c:3) noted that ‘advanced economies are currently on an unsustainable path’, and that 'significant fiscal adjustment will be essential to ensure debt sustainability’, the primary means by which, it was suggested, was to contain spending in areas related to aging related pressures, most notably healthcare. Secondly, it was suggested that economic growth would be essential in restoring the solvency of sovereigns, and it was here that the IMF placed particular emphasis on labour market reforms.

Fiscal measures to control aging related spending pressures

The 2010 Fiscal Monitor noted that many advanced economies entered the downturn with relatively weak structural fiscal positions which were further eroded not only by fiscal measures, but by underlying spending pressures. Indeed, prior to, but increasingly so since the beginning of the downturn the IMF has couched concerns regarding government debt and contingent liabilities within broader developments taking place in the context of long-run fiscal challenges related to aging-related spending, most notably healthcare.

In doing so, it was suggested that without reform these ‘could amount to more than ten times the costs of the crisis’ (Fiscal Monitor, 2009:17; Cottarelli, 2008, FAD, 2009, 2010; Freedman et al, 2009:43). Indeed, the Fiscal Monitor (2011:20) noted that ‘rising spending on healthcare is the main risk to fiscal sustainability, with an impact on long-run debt ratios that, absent reforms, will dwarf that of the financial crisis’, yet addressing such pressures would go a long way to allaying market concerns about fiscal sustainability.

The scale of adjustment required to restore debt-to-GDP levels were therefore understood as having exacerbated the need for interventions to stem unsustainable current trends. Indeed, Strauss-Kahn (2010:2) noted that reforming health entitlement constituted a key element in the quest to restore fiscal sustainability, a point iterated by Lipsky (2011) who stated that ‘to be credible, any advanced economy fiscal consolidation strategy must deal with the cost of entitlements that are a – if not the – key driver of long-term spending’.

Together therefore, an assertion was made that policies, currently constituted, could not continue to provide the benefits to citizens if nothing was done, and that, while ensuring continued access to high-quality healthcare, entitlement reforms would be critical.

Against this backdrop, the Fiscal Monitor (2011) explored a variety of means of containing spending. These included: budget caps (budget constraints and government oversight); public management coordination (referrals for accessing specialised care); market mechanisms (competition among insurers and providers); demand side reforms (expanding private insurance and cost sharing); and supply controls (the regulation of the workforce).

Of these, the Fiscal Monitor (2011:66) noted that reforms of the market mechanism were most powerful, yielding a reduction in spending of 0.5 percent of GDP, with demand and supply reforms yielding the least efficacious results. Crucially, an assumption was made that such reforms need not adversely affect health outcomes as ‘most micro-level efficiency reforms, such as the introduction of competition can improve the responsiveness of the health system to patients, but also reduce the growth of spending’ (Fiscal Monitor, 2011:9).

Moreover, although scarcely mentioned in research on its call for fiscal adjustment, the IMF has in fact sought to go even further in entrenching adjustment in the broader context of there being needed to be grounded in fiscal rules and institutions. Doing so is consistent with G20 assumptions that ‘strengthened budgetary frameworks and institutions can help to underpin the credibility of consolidation strategies’ (G20, 2010:12).

In particular, it has been suggested that the financial and economic downturn exposed short-comings in fiscal transparency standards and accounts in advanced economies which resulted in large unreported deficits and debt (IMF, 2013b:37). Credibility was therefore considered essential to anchor longer-run expectations about government solvency, hence the renewed emphasis within the IMF on fiscal rules, ‘a permanent constraint on fiscal policy through simple numerical limits on budgetary aggregates’ (FAD, 2009:4).

In doing so, the FAD (2009:15-16) noted that fiscal rules are associated with improved fiscal performance. In particular, it was suggested that: fiscal rules are correlated with stronger cyclically adjusted primary balances; budget balance and debt rules in particular contribute to improved outcomes; rules implemented at higher levels of government are associated with greater fiscal discipline than those applied locally; and some design features have a noticeably beneficial impact including those with a strong legal basis and strict enforcement.

Moreover, in addition to fiscal rules, Lipsky (2011:6) suggested that ‘good institutions are needed to underpin good policy’. In the fiscal area, institutions such as independent fiscal councils, using fiscal rules, strong medium-term fiscal frameworks, close monitoring of out-turns, and coordination have been posited as keys to success with Lagarde for example (2012b:3) noting that successful fiscal adjustment is easier with proper fiscal institutions.

The assumption was that fiscal institutions can help to exert a positive effect on public finances by: building confidence and credibility; contributing to greater fiscal transparency;

helping to monitor compliance; raising voters' awareness of certain policy paths; influencing public debates through communications and formal appearances before parliamentary committees; and providing or publically assessing macro-economic and budgetary forecasts to be used for budget preparation (FAD, 2009; Fiscal Monitor, 2010, 2012; IMF, 2013b).

Aging-related spending pressures were not a concern in previous cases of major fiscal adjustment. Policies to mitigate for the effects of the present demographic trend therefore make specific policy prescriptions somewhat novel and difficult to compare. Nevertheless, the broader context within which measures have been framed can be seen as being very much consistent with the assumptions of the neoliberal economic philosophy in the IMF.

In doing, so this approach can be understood as being problematic for two reasons. Firstly, Chowdhury and Islam (2012) have noted there are deleterious consequences to rule-based policymaking that risk democracy and development. On the one hand, in a reflection of its grounding in the neoliberal economic philosophy, the underlying rationale for fiscal rules lies, in a deep distrust in, and the need to contain the size of, government (FAD, 2009:6).

Indeed, the Fiscal Monitor (2011) acknowledged reforms would have broader implications for the role of the state in the provision of healthcare and the range of services/products financed by the public sector. This reflected the assumption made prior to the downturn in a Policy Pamphlet (IMF, 2006:41) which highlighted that the kind of reforms advocated in the health-care sector 'requires asking basic questions about whether government activities are needed, should be provided by the public sector, or could be made market based'. The corollary was calls for 'an expansion of the role of the private sector' (Fiscal Monitor, 2011:70, 2014) to remedy for inefficiencies that accompany government interventions.

Premised on the assumption therefore that 'an overblown and poorly managed public sector can result in sizable inefficiencies and crowd out private sector employment' (Fiscal Monitor, 2014:26), particularly in the healthcare sector, an explicit assumption was made that the private sector continued to provide the sole model for the efficient management of scarce resources. Indeed, the proposed imposition of the healthcare sector as a private good – a commodity – implied that it should be traded in the market place like other commodities, with state subsidies/controls that distort the market being eliminated.

Fiscal rules can therefore be understood as an attempt to depoliticise the policy framework, a move necessary to eliminate discretionary intervention by politicians. This is posited here as problematic however as it has the potential to undermine democratic governance by distorting political discourse as elections are fought on competing attempts to demonstrate a party's commitment to "sound" finance, not on who has a better social programme.

On the other hand the primary concern with fiscal policy in the IMF is sustainability, the aim being to develop credible strategies to strengthen public finances which basically relates to budgetary aggregates. Doing so ignores fiscal policy's developmental role by assuming that fiscal sustainability is a necessary and sufficient condition for growth and poverty reduction.

Indeed the Policy Pamphlet notes that 'countries with aging populations will require two very difficult adjustments, entailing not only changes in spending patterns *but also in the promises that governments make'* (IMF, 2006:43, emphasis added).

This view is clearly influenced by, and located within, the neoliberal economic philosophy in deferring to the notion that, without fiscal rules, deficits crowd out private investment and/or are offset by greater savings by private actors in anticipation of future tax rises. However, the stabilization view still dominates policy discourse. Indeed, Chowdhury and Islam (2012:4) note that this raises a fundamental question, whether the policymaking process should become hostage to the confidence game in which evidence-based policy-making is replaced by amateur psychologists seeking to read the minds of markets.

Secondly, one of the core characteristics of the neoliberal economic philosophy is the desire to separate the economic realm from the political, the most important manifestation of which has been to advocate placing control of monetary policy instruments in the hands of autonomous central bankers rather than those of elected politicians. The assumption was that it was better to leave decision-making to technocrats guided by supposedly impartial rules rather than let politicians make decisions based on short-term political calculations.

In a similar vein, Burnham (2001:1) notes that the common motive for fiscal institutions 'is a desire to adopt the good experiences of independent central banking to the fiscal sphere'. Therefore, although not wholly analogous to the function of central banking, the rationale behind the proposed adoption of fiscal institutions exhibits a number similar characteristics.

Research such as that conducted by Ebeke and Olcer (2013) for example represents part of a growing literature assessing the detrimental effects of fiscal policy volatility on long-term growth and aggregate welfare. In doing so, the authors find that during election years, government consumption significantly increases and leads to higher fiscal deficits as re-election minded incumbents use fiscal policy to satisfy the median voter, despite the potentially adverse effects on fiscal sustainability and macro-economic stability.

This has provided a motivating factor behind calls for the development of fiscal councils within the IMF, namely, to remove the political character of decision-making. In doing so, although state managers would retain arms length control over crucial economic and social processes, the assumption was that governments would benefit from the distancing effects of de-politicization, and markets would benefit from the credibility of policymaking.

In reality however Flinders and Buller (2006) have noted that de-politicization is a misnomer as the role of politics remains almost as pronounced as it would be in the absence of de-politicization, it is simply the arena or processes through which decisions are taken that is altered. Should we accept this premise then the strategy invoked by the IMF can be seen as an attempt to entrench, in the context of fiscal policy, neoliberal institutional reforms, that is, the constitutionalization of fiscal policy-making through the use of rules and councils.

Consequently, the procedures referred to as being under the rubric of de-politicization might not accurately be described as being any less political through the application of de-politicization tactics. The FAD (2009:5) for example highlighted four rules that contribute to the fiscal sustainability: *budget balance rules*; d*ebt rules*; *expenditure rules*; and *revenue rules*. Ascertaining which one, or collection would be subject to de-politicization and be embedded in an institutional framework is an inherently political exercise, left as it is to politicians to decide what functions should be de-politicized, with what tools and tactics.

Providing the foundations for growth: Accompanying structural reforms

In addition to addressing measures necessary for fiscal adjustment, the G20 2009 Pittsburgh Leaders Statement noted the need for ‘decisive progress on structural reforms that foster private demand and strengthen long-run growth potential' (G20, 2009a:2). This was iterated in the G20 Toronto Declaration in June 2010 which, drawing on IMF research, suggested that the implementation of ambitious reforms would, over the medium term: increase global output by almost $4 trillion; create tens of millions of jobs; lift even more people out of poverty (G20, 2010:2), and have a substantial impact on economic growth and welfare.

Blanchard and Cottarelli (2010:3) therefore stated that the debt crisis presented an opportunity to implement a wider set of structural reforms to boost growth, suggesting that it had the potential to exert 'a staggering effect on public debt reduction'. Indeed, Cottarelli and Jaramillo (2012:14) noted that 'history confirms that fiscal adjustment rarely occurs without healthy economic growth', a point iterated by Strauss-Khan (2010:2) who observed that no, or only minimal growth, increasingly constituted 'the biggest threat to fiscal sustainability' (see also Borg &Lagarde, 2012; Cottarelli, 2012; FAD, 2010; Lagarde, 2013).

In particular however, the discourse coordinated by the G20 and IMF stressed - thanks to the substantial margins of unused capacity brought about by what was increasingly referred to as the Great Recession (Lipsky, 2011a; IMF, 2013f) which gave rise to sluggish job growth and high unemployment in advanced economies - the need for labour market reforms.

The most comprehensive analysis of the impact of the downturn on unemployment was an IMF Policy Paper titled 'Jobs and growth: Analytical and operational considerations for the Fund' (IMF, 2013f). Here, research noted the presence of (in addition to low output brought about by the Great Recession), 'global megatrends that are influencing developments in jobs and growth' (IMF, 2013f:5) including technological change, globalization, and the doubling of the global workforce as China and India opened up in the 1980s and 1990s.

In light of these trends the IMF (2013f:7) suggested a consensus among economists that, rather than taking an active role in the provision of employment like Keynesians, the best states could do was provide a facilitating environment for growth which was considered 'an essential pre-requisite for job creation and social cohesion', inasmuch as it fostered inclusive growth, and contributed to significant reductions in poverty and inequality.

In a manner consistent with the neoliberal economic philosophy, this approach suggested only a minimal role for government which would be limited to providing economic fundamentals including an enabling business environment, and making sure that labour policies did not undermine job creation. Particular emphasis however was placed upon the provision of 'sound macro-economic policies – low inflation and sustainable public finances and external positions – as the foundation for growth and jobs' (IMF, 2013f:41).

On the question of whether there was a specific need for a job strategy over and above a growth strategy, an assertion was made that it is conventional to focus on economic growth as a precondition for employment rather than attempting to tackle unemployment directly, an approach which had proved so successful in East Asia.

This hands-off approach notwithstanding, the IMF did not have nothing to say regards the appropriate form that labour markets should take. Rather, it was noted that, given over-arching megatrends, it would be less efficient to protect people adversely affected by these changes and that the aim should be to 'protect workers, not jobs'. The assumption was that protecting jobs that were no longer economically viable through employment protection legislation would simply freeze an inefficient allocation of resources (IMF, 2013f:17).

Rather, it was suggested that workers should be protected through unemployment insurance (referred to as 'flexicurity'). Indeed, evidence presented (IMF, 2013f:21) observed that in light of global megatrends, 'there is a role for employment protection, but it should be limited' as high employment protection levels led to high unemployment durations.

Although it was acknowledged that the benefits of 'flexicurity' may take time to materialise, and have adverse short-term effects, it was suggested that those finding themselves out of work as a result should be provided with minimal safety nets and be incentivised to work through the provision of childcare and benefits commensurate with searching for work.

This approach could scarcely be more distinguishable from Keynesian economic ideas, at the heart of which was 'a pledge to secure full employment… through adroit use of fiscal policy to boost demand when recession threatened' (Wilson & Grant, 2011:3). In doing so, states worked in conjunction with business and trade unions in tri-partite structures to protect citizens through social safety nets, reducing the costs of unemployment and old age.

This largely “hands-off” approach can be considered somewhat puzzling given that fiscal consolidations tend to increase income inequality, including through their effects on un-employment, and to the extent that fiscal consolidation raises unemployment, it constitutes an important channel through which consolidation affects inequality. Indeed, it was noted that loosely speaking, about 15-20 percent of the overall increase in inequality due to fiscal consolidation may be occurring via the increase in unemployment (Woo et al, 2013:3).

The negative consequences associated with labour market reforms were not missed by senior members of the IMF. They were however, considered a necessary means by which to ensure medium to longer term prosperity. Lagarde (2012a:6) for example observed that ‘as countries undertake the sometimes wrenching reforms that are needed, the social fabric is in danger of being stretched’ as ‘in many cases, it involves lowering labour costs’, albeit this was assumed necessary as ‘reform is essential for competitiveness and for creating greater job opportunities in future’ (see also Cottarelli, 2013a; Fiscal Monitor, 2010).

The lowering of labour costs in particular was consistent however with the kind of austerity advocated by the IMF in the Latin American debt crisis and AFC in which labour costs were reduced to improve competitiveness and growth. Its advocacy in the current context was however, completely at odds with comments made by Lagarde (2012a:6) who suggested that ‘a more equitable distribution of income can help promote economic and financial stability, and more lasting growth’, and latterly, that fairness was important as ‘adjustment usually means taking tough decisions. But it should be done in a way that protects the poor and most vulnerable and shares the burden fairly across the population’ (Lagarde, 2012b:3).

Consequences for reforms

Despite stating that reforms would be beneficial at the aggregate level, short of one notable exception (Woo et al, 2013) which highlighted that spending-based consolidations tend to significantly worsen inequality, little systematic analysis has in fact been undertaken in the IMF of the distributional consequences associated with adjustment policies and structural reforms. Rather, reference has simply been made to the fact that it remains important to protect the poorest and most vulnerable members of society through minimal safety nets.

Even in Woo et al (2013) however, missing from the analysis was a systematic discussion of why debt became as large as it did and who should bear the brunt of adjustment. This is important however as, in the essence of fairness, this should offer plausible direction as to where the costs of adjustment should fall, who should bear the burden of adjustment and what are the associated distributional consequences that adjustment would bring.

Indeed, given that the downturn originated in the financial sector and required significant bank bail-outs (the first phase), subsequently infiltrated the broader economy, thereby requiring the deployment of significant fiscal stimulus (the second phase), it seems almost perverse to say the least that responses to the third phase (an amalgam of the fiscal costs of the first two phases and the accompanying recession which brought about sovereign debt sustainability concerns) took the form they did; that is, the postulated necessity of the further entrenching of structural reform policies in healthcare and labour markets in a manner that strengthened rather than fundamentally challenged neoliberal economic ideas.

This begs the question however of how the narrative underpinning this policy shift changed so fundamentally. Here the manner in which the IMF framed the third phase had a crucial part to play. Brandwein (2006:230) has noted that understanding how an event is framed requires the analytical isolation of taken-for-granted assumptions as these help us to understand why subsequent action is taken. Indeed it was here that, despite the fact that a number of assumptions had been discredited, cognitively speaking, during the second phase of the downturn, the IMF never abandoned its normative commitment to the neoliberal economic philosophy which privileged the importance of fiscal sustainability, and it was these assumptions that helped to shape the IMF understanding of the third phase as one of excessive sovereign debt requiring fiscal adjustment and structural reforms.

Moreover, in addition to providing the cognitive ideas underpinning this shift, so too did the IMF couch the need for reforms in explicitly normative terms. In doing so, a suggestion was made that fiscal adjustment and structural reforms were a necessary penance to be paid by states and the public for their pre-crisis fiscal profligacy. This was exemplified by Lagarde (2012b:2) who suggested that ‘we can’t pin the blame for our fiscal woes on the crisis alone... as the public debt ratio was already at a post-war peak by 2007’, and iterated by Blanchard and Cottarelli (2010:2) who noted that excessive fiscal burdens ‘are due not only to the crisis, but also how fiscal policy was mismanaged during the good times’.

Against this backdrop, the IMF was able to construct a narrative, consistent with neoliberal economic ideas, which drew on the appeal of the need for fiscal adjustment through reference to a series of apparent “truisms” which included the notion of not spending more than you have; of living within your means, that proved especially intuitive.

Indeed, that the IMF, working alongside the G20, was so readily able to construct such a narrative demonstrates the importance of politics in the process of crisis narration. That is, the sovereign debt burdens were brought about by banking and financial sector pathologies which spilled over into the real economy, negatively affecting economic growth and employment the world over. It was not a sovereign debt crisis generated by excessive spending for anyone other than perhaps the Greeks, and it was certainly not the result of unsustainable aging-related and labour market policies. That it has been couched in such terms however, suggests a politics of ‘bait and switch’ (Blyth, 2013:5).

This was a point iterated by Gamble (2014:157) who observed that the losses incurred by sovereigns bearing the fiscal impact of the downturn were drawn upon in order ‘to frame the political debate about austerity, the need for belt-tightening and shrinking the size of the state’. The problem with this approach however is that ‘to suggest this is a fiscal crisis *of* the state would be to implicate the state directly in the generation of the fiscal shortfall that threatens the public programmes with which we associate it’ (Hay, 2013:8).

However, should we recognise the problem as a fiscal crisis *for* the state is to make no such assumption. Indeed, it is to suggest that the sovereign debt which now threats public expenditure and associated growth-related policies cannot be attributed to any dynamic internal to the state its self since its origins have been shown to lie elsewhere (Hay, 2013:8). Viewed in such a manner we can see how, had the third phase of the downturn been framed differently, we change our sense not only of the problems, but we also change the range of responses that would be considered both necessary and desirable.

Therefore that sovereign debt levels were framed as problematic and requiring intervention was clearly not a politically neutral process, but can be more accurately conceptualised as a process of strategic social construction by the IMF. In doing so, the diagnosis came with a set of accompanying policies, including an opportunity to reform un-sustainable aging-related policies through spending constraint as well as a chance ‘to implement difficult, but needed, structural reforms' under the guise of boosting GDP (Anderson et al, 2014:1).

This adjustment-cum-growth objective however, while broad, represented a specific attempt, to implement policies geared towards: strengthening market incentives and raising efficiency; boosting sustainable growth; and increasing the role of market and competition in the economy through the implementation of policies consistent with the prevailing economic philosophy. Together, this demonstrates how the IMF continues to retain a normative commitment to free market outcomes through reduced government intervention.

Concluding remarks

Chapter 4 demonstrated how, during its initial phase, problems were manifest primarily in the banking and financial sectors, and a relative slowdown in economic growth. As a result, the IMF advocated a range of policies to remedy for the unfolding pathologies that were derived from the neoliberal frames of reference. These included lowering policy rates, extending the provision of central bank liquidity, and latterly, forward guidance of the policy rate along with large scale asset purchases by central banks.

Given the inability of monetary policy in both its conventional and unconventional guises however to prevent the transmission of the downturn to the broader economy (the second phase) the IMF advocated an altogether different set of policy interventions. This included, most notably, substantial discretionary fiscal stimulus to increase aggregate consumption by supporting domestic demand. It was this move in particular that led to suggestions of a potentially epoch-shaping shift away from neoliberal economic ideas in the IMF.

This notwithstanding, this chapter has suggested that that change which has occurred has been largely limited, having not been accompanied by a more fundamental shift in the prevailing economic philosophy or the way in which economic problems are interpreted and responded to. Indeed, as the downturn unfolded and entered its third stage (a concern in the IMF with the implications of increasing sovereign debt burdens), the manner in which the downturn was interpreted and responded to suggested that the IMF in fact continued to exhibit a normative commitment to neoliberal economic ideas. That is, this phase was couched in a broader context in which more policies consistent with neoliberal economic ideas, not those diverging substantially from it, were required, not less.

Chapter 6

Financial sector liberalization I

'It is a world of change in which we live' (Frank Knight)

Introduction

This chapter serves two purposes. On the one hand it is shown how the decision to allow banks to increase leverage and lower capital buffers was clearly misguided as the downturn demonstrated their susceptibility to declines in asset prices. During the first phase (understood here as running from summer 2007 to autumn 2008), responses centred on calls for a financial system characterised by less leverage and greater capital ratios in order to mitigate risk taking and absorb losses when they do occur, a commitment framed in the broader context of the need for greater supervision of the implementation of the pre-existing Basel 2 capital accords. As a result, neoliberal economic ideas in the IMF are shown as being characterised by a considerable degree of continuity, with banking and financial sector pathologies postulated as being resolvable within existing frames of reference.

On the other hand, it is suggested that as the banking and financial turbulence spilled over into the real economy, particularly in autumn 2008 (the second phase) it became apparent that simply implementing the existing Basel accords would be insufficient and that more substantive regulatory reform was required. Attention therefore turned to the creation of a new set of rules (Basel 3) that doubled capital requirements and introduced conservation and counter-cyclical buffers. This shift from a micro- to complementary micro-/macro-prudential (MicPR/MacPR) approach, giving states considerable scope to intervene in baking/financial sectors, appeared, superficially at least, to have marked a crucial shift in neoliberal economic ideas in the IMF which had rested on an assumption that financial markets, left to their own devices, would be both efficient and self-equilibrating.

Notwithstanding this ostensible shift, Chapter 7 suggests that as the third phase of the downturn began in winter 2009, it became evident that actual reforms were not as fundamental as it was initially envisaged they might be. Rather, it is demonstrated that, despite some change in the kinds of policies now on the table for discussion, reforms continued to be couched within the neoliberal economic philosophy that prevailed prior.

As was the case in Chapters 4 and 5 the means by which this is assessed is through a text analysis of research produced by knowledge-based experts within the IMF which has, along with the FSF/FSB under the guidance of the G20, sought, through the coordinative discourse to produce research in order to influence the direction of the capital adequacy debate.

These include the bi-annual reports WEO and GFSR, along with Working Papers, Staff Discussion Notes and Policy Papers produced by members of the Monetary and Capital Markets Department (MCMD) (its aim being to be a centre of excellence for all aspects of financial, capital market, and monetary policy in the IMF) which communicate the economic ideas that underpin economic philosophies, problem definitions and policy priorities. This includes MCMD Directors Jaime Caruana and latterly Jose Vinals, senior MCMD staff Laura Kodres and Iditya Narain and others, and Research Director Olivier Blanchard.

This research is therefore especially important for our purposes as it is here that the IMF seeks to persuade policymakers and practitioners that economic ideas constituting the coordinative discourse are both necessary (cognitively) and appropriate (normatively).

Operating on the assumption however that research not only contributes to the process by which actors are persuaded of the benefits or otherwise of a certain course of action, both this chapter and the next also incorporate the means by which new knowledge is drawn on, and communicated through, speeches by senior IMF officials who offer another important source by which to gauge the IMFs interpretation of, and responses to, the downturn. This includes Managing Director Dominique Strauss-Kahn and latterly Christine Lagarde, First Deputy Managing Director John Lipsky, and Research Director Olivier Blanchard.

Phase 1: Banking and financial sector turbulence and the shift to greater capital adequacy

In the run-up to the banking and financial sector turbulence academics, the banking sector, government officials, and international financial institutions including the IMF and Financial Stability Forum (FSF) (incorporating national financial authorities, BIS, World Bank, and others) exhibited an inter-subjectively held consensus regards the capacity of banking and financial institutions to manage their own risks and regulate themselves effectively.

Indeed, so pervasive and entrenched had the assumed efficacy of financial markets become that, in the run up to the first phase of the downturn regulators and supervisors failed to acknowledge and counter the incentives of leveraged financial institutions to take excessive risks through the more effective deployment of existing supervisory tools. As a result, banks financed their portfolios with less capital, thereby increasing the rate of return, reduced capital by moving assets off balance sheets in “structured investment vehicles”, and at times, actively sought both to deceive regulators about the levels of capital they were holding and the way in which they were undertaking their risk assessments.

Blanchard (2009:8) for example noted that in 2006 the value of off-balance-sheet assets of Citigroup ($2.1 trillion) exceeded the value of assets on the balance sheet ($1.8 trillion). This practice was not simply limited to banks however as, in late 2006, mono-line insurers (those insuring against a particular risk), operating outside the perimeter of regulation, had capital equal to $34 billion to back insurance claims of over $3 trillion worth of assets.

The implications were obvious. If the value of assets declined and/or became uncertain, the higher the leverage, the higher the probability that institutions would become insolvent. This is exactly what happened as, beginning in the summer of 2007, financial institutions that had invested heavily in securities linked to sub-prime mortgages faced enormous losses as international financial markets began to freeze up, thereby further compounding difficulties in institutions that were highly leveraged, under-capitalised and dependant on short-term funding. Moreover, equally as pertinent was the fact that uncertainty about the location of losses and the valuation of other assets led financial markets to panic further.

The first phase of the downturn therefore demonstrated that, under the existing regime, in good times, capital inadequacy prevailed as risk sensitivity became dulled and measured risks appeared to be reduced. Senior Financial Sector Expert of the MCMD Sacasa (2008:4) for example noted how risk-based capital requirements were susceptible to erosion in the good times as risk measures tend to ignore risk build-up during upswings. This allowed lenders to increase leverage and credit, thereby reinforcing asset price increases, which ultimately generated a self-feeding spiral between leverage and asset prices.

Conversely, when risk measures mount during down-swings and losses materialise, capital buffers insufficiently built-up during good times are eroded and are not easily replenished since external capital becomes increasingly scarce. Interactions between capital, credit, and asset markets can then magnify the turmoil by forcing chain reactions of asset sales, a self-reinforcing credit crunch and contracting economic activity. Together therefore, not only did regulatory rules not dampen pro-cyclicality in financial markets, they actually aggravated financial sector pathologies as banks held more capital as risk increased (while capital was already depleted), forcing them to cut back on lending, so worsening the initial downturn.

Finally, had the implications of capital *in*adequacy been limited to individual banks, the impact on the broader financial system would not have been so pronounced. Nevertheless, the banking and financial sector turbulence drew attention to the spill-over problems that existing policies had played in contributing not only to local, but to broader systemic risk.

Problem definition

The banking and financial sectors at this juncture were clearly operating in a context of increasing uncertainty as many cognitive assumptions held regarding the efficacy of freely functioning markets, along with their associated policy interventions, began to unravel.

Nevertheless, the ability to comprehend the volume of information related to banking and financial sector pathologies meant that the IMF deferred to a simplifying mechanism so as to cope with, and be better placed to process, the massive amount of incoming information. These were found in existing schemas (the neoliberal economic ideas held in the IMF) which provided a means to interpret, understand, and respond to events. Indeed, these ideas shaped the way the initial shock was interpreted and responded to (Barnett & Finnemore, 2004:9). This draws our attention to the fact that is was the economic ideas held by the IMF, not rational responses that guided the initial response to the increasing uncertainty.

These economic ideas came with an existing set of variables which privileged incoming information consistent with the extant economic philosophy and problem definitions, while also providing a template which directed the IMF towards specific examples from which similar banking and financial sector downturns could be compared and drawn upon. In doing so, the economic ideas held by the IMF were critical in shedding light on the origins and functions of lessons from the past, and coloured initial images related to the downturn.

This approach again allows us to show how the IMF attempted to reduce uncertainty, how existing economic ideas provided the means by which to relate and respond to the down-turn, and how the policies derived from the analogies invoked were ultimately insufficient. This approach stresses, in a manner consistent with Blyth (2002:52), the importance of the economic ideas held by the IMF in interpreting and responding to economic uncertainty.

During the first phase of the downturn the IMF therefore drew on the lessons of the past (or more accurately, what they thought those lessons taught them) in order to guide initial policy responses. In particular it is shown how a number of inferences were made (implicit or otherwise) through reference to historical analogies - comparing banking and financial sector turbulence with similar episodes that preceded it – in an effort to reduce uncertainty.

In doing so, the IMF invoked the lessons of the past to display the banking and financial environment as one of continuing risk as opposed to uncertainty. Indeed, by drawing on the lessons of previous episodes of financial distress it is shown how the analogies invoked by the IMF suggested that the current turbulence was comparable with a larger number of similar instances from the past, thereby making the economic environment more knowable.

Again, the means by which this was undertaken can be explained through reference to the schematic provided by Khong (1992) *AX:BX; AY:BY*. Nevertheless, in this instance *A* (banking and financial sector turbulence) resembled event *B* (previous episodes of banking and financial sector volatility) in having characteristic *X* (being brought about by an asset boom and bust); *A* had characteristic *Y* in being considered resolvable through the increased provision of information, enhanced disclosure, and more effective market discipline. So too was it therefore thought that *BY* (banking and financial sector turbulence brought about by an asset boom and bust) was resolvable through a similar set of policy interventions.

The lessons learned from the past, themselves a derivative of adherence to the frames of reference provided by neoliberal economic ideas, are shown as devices that serve three tasks: to define the problem confronting actors by comparing the situation with others with which the IMF was familiar; define the stakes; and imply policy solutions (Khong, 1992:20).

In light of this discussion we can see how a number of simplifying assumptions regarding the nature of banking and financial sector pathologies, interpreted as analogous to other like-instances preceding it, were made that meant the unfolding turbulence could be treated in a similar manner. Indeed, one of the key lessons drawn by the IMF was that, just as they had in previous financial crises, undercapitalised financial institutions had played a crucial role in initiating/exacerbating financial sector turbulence, thereby demonstrating that the existing approach to capital regulation (the funds required to absorb losses) was inadequate.

In order to persuade others of the appropriateness of this diagnosis, two arguments were advanced that underpinned calls in the IMF for more and better quality capital. The first noted that capital is a buffer that absorbs losses and reduces the risk of insolvency, so mitigating risk factors such as collective uncertainty over counterparty risk which had a major propagation effect. The second argued that capital reduces limited liability-driven incentives of banks to take excessive risk by increasing their "skin-in-the-game".

Although there were several ways to mitigate this problem the most simple it was suggested (see for example GFSR, 2008; GFSR, 2008a; Sacasa 2008; WEO, 2008a), was to make capital requirements counter-cyclical – the amount of capital needed to support given assets would rise during booms and fall during busts. Doing so, it was thought, would mitigate for the fact that existing rules/practices were backward-looking, recognising risks too late, yet making capital adequacy requirements counter-cyclical would better reflect "through-the-cycle" risks, limiting pro-cyclicality; and enable supervisors to resist pressures from politicians or firms to let things continue on an upward trajectory without acknowledging that leveraged institutions had incentives to take on excessive risks without internalising systemic risk.

The acknowledgement of the failure of capital standards notwithstanding, there was still a sense within the IMF that the overall regulatory framework had not been fundamentally damaged, a point made by Strauss-Kahn (2011a:2) who retrospectively noted that the first phase was considered by many a failure of supervision as opposed to regulation.

This was demonstrable in, for example, an April 2008 IMF paper (IMF, 2008:1-2) seeking to draw tentative lessons from the early stages of the downturn which noted that supervisory failures were particularly evident in: scrutinising risk management practices; not adequately accounting for risks associated with new financial instruments; and their failure to address gaps associated with the valuation and financial reporting of structured products.

Indeed, so much faith had been placed in the ability of financial institutions to manage their own risk portfolios that interpreting the unfolding banking and financial turbulence as one of regulatory as opposed to supervisory failure would have contradicted one of the key neo-liberal economic ideas; that markets were self-regulating and tended towards equilibrium.

Viewed through the lens of supervisory as opposed to regulatory failings however, implied that all that was necessary to rid the banking and financial sector of their pathologies was intervention in the form of the greater supervision of existing regulations which was now considered the predominant challenge for regulators and supervisors. Interpreted in such a manner, substantive regulatory change was considered neither desirable nor necessary.

Rather, an assumption was made that stronger supervision would mitigate for the fact that: supervision in the run-up to the downturn was weak in independence and accountability, industry or political capture, wrong incentive structures provided by politicians, lack of will to probe or take matters to their conclusion, a misalignment of incentives for supervisors to voluntarily cooperate, along with a lack of binding coordinating mechanisms.

To remedy for the misalignment of incentives a paper produced by the MCMD (2008) noted that, in order to be effective, supervisors required: a mandate to enforce existing laws and regulations; the ability to investigate breaches of laws/regulations; and the authority to bring charges and impose sanctions as in their absence enforcement was meaningless. Indeed, of existing regulations Carvajal and Elliott (2009:20) of the MCMD noted that ‘it is not the law, but the implementation and enforcement of the law’ that was most important.

For this reason, Cortavarria et al (2009:12) of the MCMD cautioned against an immediate and unnecessary move from a discretionary to stronger system of rules-based policymaking. The argument being that the prevailing regulatory framework already afforded supervisors considerable discretion to implement a range of policies, but that the downturn highlighted that policymakers can be reluctant or slow to act. Accordingly, the authors advocated the need to better implement existing rules rather than rushing to re-regulate un-necessarily.

Together, these calls were premised in large part on an assumption that the global economy was characterised not by uncertainty, but by risk, which continued to be an inherent, and important, part of the financial landscape. Therefore, indiscriminately expanding the scope of regulation with the aim of reducing pro-cyclicality and eliminating risk-taking altogether was considered unnecessary, if not deleterious. Rather, the IMF continued to advocate the need to balance reducing pro-cyclicality with the need to adequately reflect financial risks.

Policy implications

Interpreting banking and financial sector turbulence in the manner that it did meant that, despite acknowledging the need for stronger capital standards, initial policy prescriptions did not differ significantly from those already in place. Rather, the analogies invoked directed policymakers to define the problem in line with the frames of reference provided by neoliberal economic ideas, a move which introduced choice propensities into policymaking, directing the IMF towards particular policy avenues at the expense of others.

In doing so, the policies advocated by the IMF continued to be derived from the extant Basel 2 capital adequacy framework. Assumed as a significant improvement over its predecessor, Basel 1, under which banks were able to circumvent capital requirements insensitive to risk, it was thought Basel 2 would lead to financial stability through better risk management, supervision, and market discipline. The IMF (2008:6) therefore suggested that, implemented rigorously, Basel 2 already provided sufficient scope for improvements in bank regulation, and especially so in terms of the required capital buffers. This was supported by the FSF (2008:12) which suggested that Basel 2 was a ‘starting point for improving major banks’ and securities firms’ capital adequacy’ standards and as a result ‘needs timely implementation’.

This assumption was echoed by MCMD Director Jaime Caruana (2007:1) who in a December 2007 speech noted that ‘this is the time to implement Basel 2’ as it was already making a positive contribution in addressing risks facing banks. Indeed, Caruana and Narain (2008:1), along with the FSF (2008:12), noted that banking and financial sector turbulence had effectively occurred during Basel 1 as Basel 2 was incompletely implemented. Although not able to prevent the turbulence, Caruana suggested that had Basel 2 been implemented in all affected jurisdictions prior, the virulence could have played out far less virulently than it did.

Implications for the neoliberal economic philosophy

Consistent with the fact that there was no significant shift in the way economic problems were interpreted, so too, was there no shift in the policies advocated to mitigate for the unfolding turbulence. Moreover there was no shift from the neoliberal economic philosophy in the IMF, which continued to exhibit a belief in the ability of markets to self-regulate. Rather, the initial manner in which the prevailing problem was interpreted, along with the kinds of policies advocated both within the IMF and FSF, were narrowly focused on the production of 'recommendations for increasing the resilience of markets and institutions' (FSF, 2008:1) as opposed to fundamentally challenging their inherent efficacy.

Indeed, there was still an assumption within the IMF that the banking and financial sectors (i.e. the private sector) would continue to play a significant role in remedying unravelling pathologies. This was a point echoed by Moschella (2010:137) who similarly observed that during its first phase, the IMF 'still acknowledged that the private sector had a central responsibility in the good functioning of financial markets', which perpetuated the notion of markets as self-equilibrating and efficient (Kessler, 2012:276).

So, for example, despite the postulated benefits of the successful implementation of Basel 2, the continued deference of the IMF to the perceived efficacy of the market should not have been entirely surprising. Rather, Basel 2 was very much conceived in institutions of global economic governance characterised by a distinctively neoliberal political economy which had placed a considerable degree of emphasis on belief in the efficacy of markets.

Therefore, although calling for the implementation of Basel 2, Caruana (2007:2) himself noted that 'supervisors should not be telling banks how to manage their business... that was the spirit of the intensive consultation and dialogue between the industry and supervisors during the Basel 2 process'. This assumption was shared by the FSF (2008:10) which noted that it remained 'the responsibility of firms' board and senior management to manage the risks they bear', not regulators. Indeed, Caruana suggested that Basel 2 was a regulatory capital framework, not an overall guide to how banks should run their businesses, and as a result, they would not prevent banks from making mistakes – or substitute for banks' own responsibilities for assessing and managing their individual risk portfolios.

Moreover, Caruana (2007:2) noted that the current problems in the banking and financial sectors went far beyond the objectives of a capital adequacy framework and that Basel 2 should not be considered a panacea for all financial market troubles. Rather, its aim was limited to removing pro-cyclicality without completely negating risk-based decision-making.

It was in a similar vein that in a 2008 paper (IMF, 2008b:4-9) drawing tentative lessons from the first phase of the downturn, the IMF suggested that: it should be within the purview of managers, not state regulators to challenge assumptions underlying risk models; attention should be paid to the robustness of hedging strategies and understanding a firms broader exposures; supervisors should encourage managers to conduct more rigorous stress testing; and risk management cannot be achieved solely by regulation, rather the onus remained on senior management in financial institutions to ensure robust internal governance structures.

Against this backdrop, IMF staff acquiesced, just as they had during previous instances of banking and financial sector turbulence, to the prevailing economic philosophy which suggested the best policymakers could do was call for the collection and dissemination of more and better information, and the improved disclosure of risks which together would mitigate for increasing uncertainty. Doing so it was suggested, would restore confidence in the financial system regarding the prices of assets and balance sheet losses, thereby staving off broader systemic threats. A number of policies were advocated in a joint September 2008 IMF/FSF paper seeking to draw lessons from the banking and financial turbulence, all of which were broadly similar to those advocated in the context of the AFC (see Chapter 2).

The take-home message was the need for: greater transparency in the banking and financial sectors; the provision of better and timelier information; better crisis response mechanisms, and arrangements for dealing with financial system stress. The assumption was that doing so would allow market actors to see the world as it really was, thereby helping to transfer incalculable uncertainties into a calculable and knowable economic environment. Indeed, this paper observed between the IMF and FSF at this juncture 'a considerable degree of consistency between these recommendations and the preliminary policy lessons from the crisis formulated by the Fund' (IMF/FSF, 2008:6; see also GFSR, 2007a).

Therefore, just as previous episodes of banking and financial sector stress were understood as having been brought about and/or exacerbated, by inadequate information, transparency and disclosure which had hampered effective market discipline, so again was it suggested that their increased provision, all of which were instantiated in Basel 2, would be sufficient to remedy for the effects of the current downturn. Framed in such a manner, and having been viewed as analogous to similar instances that had preceded it, we can see how the IMF interpretation of banking and financial sector pathologies was limited to a moment of instability puncturing what was in fact an otherwise stable economic environment.

Implications of lessons from the past for continuity in neoliberal economic ideas

It was suggested in Chapter 4 that we would not expect that the neoliberal economic ideas through which incoming information was interpreted during the initial phase of banking and financial sector turbulence be abandoned at the first sign of discrepant information as observed anomalies would lead to a search for imaginary fundamental novelties.

Indeed, Hay (2008:9) notes that we are much more likely to see the vehement reassertion and articulation of prior conceptions during the earliest stages of increased uncertainty. A similar logic can be applied here, albeit in this instance, this was arguably most relevant in the very earliest stage in which banking and financial sector pathologies were manifest.

At this juncture, to have assimilated incoming information through alternative economic ideas would have demonstrated that IMF assumptions regarding the efficacy of freely-functioning markets had fundamentally failed. Given that neoliberal economic ideas were so deeply held both in the IMF and other institutions constituting the coordinative discourse, and had played such a crucial part in underpinning the hands-off regulatory approach to modern financial risk management, this would have been a startling admission to make.

It would therefore have been premature to condemn the IMF for cognitive distortion in the very earliest stages of the banking and financial sector turbulence. Indeed, to suggest that this was the case is not the point to be made here. It is however crucial to our purposes, that as the first phase progressed, as banking and financial sector pathologies worsened, incoming information and policy responses were increasingly stretched to fit within the frames provided by neoliberal economic ideas. That is, the IMF's ability to identify mounting risks continued to be hindered by both ‘intellectual consistency’, and assumptions ‘that major financial crises in large advanced economies were unlikely' (BWP, 2011:1).

Chapter 4 observed in the case of economic policy that this was not a trait exclusive to the operational functioning of the IMF, but reflected the problems of deriving the lessons of history by reasoning through historical analogy and interpreting incoming information through existing economic ideas, and why they are so often deployed sub-optimally (Khong, 1992; Jervis, 1976; May, 1974). Three reasons as to why are particularly noteworthy.

Firstly, we can see in this instance how the lessons learned from historical analogies invoked – the assumption that just as the increased provision of information, enhanced disclosure, and more effective risk management had been considered necessary to rid the banking and financial sectors of their pathologies in previous episodes of turbulence, so too would they be sufficient again - were selected on the basis of superficial similarities which were a reflection of continuing adherence to belief in the efficacy of neoliberal economic ideas.

The result was that the requisite policy responses to the problem so-defined, were constrained from the out-set, and would therefore ultimately prove insufficient. Indeed, Brassett et al (2010:1) noted that doing so 'placed unnecessary and unhelpful restrictions on how events surrounding the subprime crisis and its associated credit crunch have unfolded'. That is, by not searching beyond superficial surface similarities, the potential for deriving less obvious lessons from more suitable analogues was inherently limited (Jervis, 1976:191).

Secondly, the information generated by the banking and financial turbulence was simply assimilated through the frames provided for by neoliberal economic ideas. This explains why the IMF was so receptive to information that appeared to confirm existing assumptions.

The corollary of this however was that information inconsistent with the existing neoliberal economic philosophy, problem definitions and policy priorities was largely marginalised as the reluctance to accept potentially contradictory evidence prevailed. Indeed, that attempts were made to fit new information in existing patterns of expectations, despite an increasing amount of discrepant information, carried with it an implicit assumption that underlying economic ideas were correct, and information to the contrary irrelevant. That is, beliefs regarding rational actors and efficient markets continued to predominate, with the need for greater transparency, and enhanced disclosure and risk management retaining primacy.

That the IMF engaged in such an endeavour was a process inherent to assimilating incoming information through the theoretical lens provided by existing economic ideas: they often persist even in the face of potential evidence pertaining to their inefficacy; and shows how the past acted as a guide for future action. Therefore rather than correct conceptions, the IMF was characterised by increasingly strained interpretations of unfolding pathologies.

As a result, although it is impossible to clearly delineate between the point at which clinging to existing neoliberal economic ideas crossed the line into simply disparaging discrepant information beyond such a point that was reasonable, it became increasingly evident that as the first phase unravelled through 2008 that IMF policy responses were incapable of dealing with the particularities of the banking and financial sector pathologies. That is, despite quite obvious defects, the IMF nevertheless continued to defer to neoliberal economic ideas.

Finally, by ignoring information that might contradict the neoliberal economic philosophy and associated problem definitions, the IMF was heavily influenced in the direction of a particular course of policy action at the expense of the many others that were available.

In doing so, the analogues invoked by the IMF meant that policies - hamstrung by existing neoliberal economic ideas and what was deemed appropriate within a narrowly defined frame of reference - failed in two key respects. Firstly, they failed to sufficiently illuminate what was unique, and particularly problematic about unfolding banking and financial sector pathologies. Secondly, this led the IMF to advocate policy actions which would ultimately prove insufficient to prevent such pathologies from worsening even further.

Indeed, proffering a particular solution in line with existing economic ideas meant that the potential for a genuine analysis of the causes of the downturn were precluded by enforcing the characterisation of banking and financial sector pathologies as abnormalities in an otherwise effectively-functioning broader economic framework. This therefore did not lead to an analysis of the extent to which the problem may well have been the very essence of contemporary banking and financial sector 'normality' its self (Brassett et al, 2010:2).

This demonstrates how, drawing on the constructivist assumption that moments of failure require endogenous interpretation as a crisis through changes in the way problems are defined and responded to (which requires the deployment of an alternative economic philosophy), no attempt was in fact made to define the pathologies afflicting banking and financial sectors as such. Rather, there was no direct sense of crisis as events were characterised by attempts by the IMF to posit the continuing efficacy of prior conceptions.

The preceding discussion therefore places us in a position to state with some conviction that responses to banking and financial sector pathologies were characterised by a considerable degree of continuity during its first phase. That is, although there was a recognised need to strengthen supervision, policy priorities continued to be derived from frames of reference provided by neoliberal economic ideas, with market-centred responses continuing to assume prominence even as banking and financial sector pathologies worsened. As a result, no fundamental argument was made for rethinking the existing economic philosophy in the IMF which continued to privilege a belief in the efficacy of freely functioning markets.

Phase 2: Problem definition

The preceding discussion notwithstanding, by autumn 2008 the Western banking system faced collapse. Banks were nationalized or part-nationalised, mergers and acquisitions were facilitated by government, while others simply collapsed into bankruptcy. That "efficient markets" suddenly found themselves requiring multi-trillion dollar bail-outs from the supposedly "irrelevant state" led Blyth (2013:208) to comment that 'if you ever wanted an empirical disconfirmation of a social science theory, this was it'.

Indeed, the very banking and private financial institutions that had argued most vociferously for market-friendly regulation suddenly found themselves on the defensive and politically weakened as those that had essentially been allowed to self regulate were now highlighted as the key culprits in triggering the turbulence. Their ability to resist stronger regulation therefore seemingly disappeared, curtailed as it was by massive reliance on state support.

The banking and financial meltdown therefore appeared likely to undermine the credibility of the neoliberal economic ideas that had played a major role in encouraging the creation of market-friendly financial standards. These included not just the free market ideology, but more technical economic concepts such as the rational expectations and efficient markets hypotheses. Indeed, the scope of the collapse suggested that the faith in markets that dominated the preceding decades had been naïve at best (Skidelsky, 2009; Soros, 2009).

The declining performance of status quo institutions and policies therefore appeared to have destabilised prior assumptions on both cognitive and normative levels. In the case of the former, inter-subjectively held beliefs regarding the efficacy of freely functioning capital markets and their ability to self-regulate could scarcely have been any more discredited. This was evident in the fact that market prices of financial assets did not reflect "correct" prices based on current information, nor did actors act on the basis of rational expectations, but on their "inter-subjective expectations" which led to a collective panic (Hall, 2009:453).

Indeed, in a 2008 speech Strauss-Kahn (2008c:1) noted that 'the heart of the economic crisis lay very much at the feet of financial markets'. This admission raised expectations that we might see the end of the neoliberal era which had privileged the market mechanism, to a paradigm that rejected the discredited intellectual orthodoxy that had dominated prior.

In the case of the latter however, there developed a broad consensus both that financial markets should not be allowed to again have the kind of adverse impact on the functioning of the real economy as they were currently, and that 'we must move away from a system that privatises the gains and socialises the losses' (Strauss-Kahn, 2010e:1).

Unlike during its first phase, as the turbulence entered its second phase (banking and financial sector pathologies implicating economic growth in the real economy), the IMF was no longer faced with an environment that could in any sense be characterised by increasing risk which it might be able to mitigate for through the increased provision of, and access to, better and/or timelier information, and more stringent supervision of existing policies.

Rather, the economic environment was characterised by a large degree of uncertainty, a situation in which although not entirely non-existent, there was no large group of similar instances on which to draw because the situation at hand was to a considerable degree unique (Knight, 1957:232-239). That is, the IMF was faced with a situation in which not only was it difficult to make probabilistic calculations of events, it was almost impossible to form any meaningful estimate of future events. Indeed, what the IMF thought it knew regards freely functioning markets had become so uncertain that it forced a fundamental re-examination of conceptions about the appropriate role and function of financial markets.

In an effort to reduce the uncertainty brought about by a moment of political-economic failure, Blyth (2007:762) suggests that competing actors typically engage in the politics of crisis construction with each seeking to persuade others ‘of the correctness of one particular diagnosis of the crisis at hand’ and the policies required to eradicate its pathologies.

In this instance however although failure in the banking and financial sectors had the potential to 'support and sustain a multitude of competing, indeed mutually incompatible, narratives' (Hay, 1999:324) of what went wrong, there developed a consensus among actors constituting the coordinative discourse, most notably the IMF and G20, that the prevailing economic narrative, centred on belief in the ability of financial markets to operate as self-maintaining entities, and the entire edifice of risk management techniques had collapsed. Indeed, Moschella (2010:141) observed among these institutions ‘a remarkable consensus on the failure of existing policies governing the function of the global financial system’ which shook the belief in the ideas behind market-led liberalization (see also Baker, 2015:352).

At the Washington leaders G20 summit in November 2008 for example, a pledge was made ‘to strengthen regulatory regimes, prudential oversight, and risk management, and ensure that all financial markets, products and participants are regulated and subject to oversight’ (G20, 2008:3). This was based on the notion that ‘major failures in the financial sector and in financial regulation and supervision’ were ‘fundamental causes of the crisis’ (G20, 2009:3).

Moreover, in the IMF, Caruana (2009:3) went from suggesting that during its first phase, markets would play a crucial part in helping to remedy for the pathologies presented by banking and financial sector turbulence, to suggesting that the scene was now set for ‘far-reaching changes in the shape and functioning of financial markets that was now needed’.

In a similar vein, in a 2008 speech Strauss-Kahn (2008d:6) observed the potential for a ‘new financial architecture’ which would reflect the collective recognition that the downturn was not just the result of inadequate supervision, but a more fundamental failure of regulation, market discipline and risk management in financial institutions. Indeed even that which was sufficient, supervisory enforcement, it was noted, could have been much stronger than “the private sector knows best” approach which had led to serious lapses in oversight in the run up to the downturn (Strauss-Kahn, 2008; 2008a; 2009; 2009a; 2009d; Blanchard, 2010).

Against this backdrop, at its Washington Summit in November 2008, the G20 noted that 'the IMF, expanded FSF, and other regulatory bodies should develop recommendations to mitigate pro-cyclicality, including the review of how valuation and leverage, bank capital, executive compensation, and provisioning practices may exacerbate cyclical trends' (G20, 2008:7). These institutions, along with the BIS, constituted the most significant actors in the coordinative discourse, their aim being to maintain global financial stability and prevent a repeat of the errors preceding the downturn by developing/overseeing the implementation of internationally-agreed regulatory banking sector policies (Vinals et al, 2010:6).

To be sure, the IMF was not at this juncture tasked with becoming a global regulator. What it did do however, given the nature of events in banking and financial systems, was begin to operate more cooperatively and collaboratively with the FSF, with their work being viewed as complementary and with mutually enforcing roles. That is, the IMF participates: on an on-going basis in meetings at the highest levels of what was renamed the Financial Stability Boards (FSB) including the Plenary (its sole decision-making body); in high-level standing committees and groups (including the steering committee); through projects and outreach efforts; and contributions to FSB papers/publications (IMF, 2008c, 2013f; IMF/FSF, 2008).

The need for greater cooperation to develop internationally-agreed standards was premised on the fact that because 'financial markets are global in scope... intensified international co-operation among regulators and strengthening of international standards, where necessary, and their consistent implementation is necessary' (G20, 2008a:2). Doing so, it was suggested would 'minimise regulatory arbitrage, promote a level playing field, and foster the widespread application of the principles of propriety' (G20, 2010:19; see also G20, 2009:3). Similarly, the Chairman of the FSF (2008) noted that a lack of trust had prompted states to safeguard their markets, yet this could be avoided if governments committed to applying global standards as this would build confidence in the quality of cross-border regulation.

With this in mind the G20 acknowledged the need to: extend regulation to all systemically important financial institutions, instruments, and markets; strengthen over-sight; improve risk management; and strengthen transparency (G20, 2009; G20, 2009a). An assumption was made however that although reform must be multi-faceted 'at its core must be stronger capital standards, complemented by clear incentives to mitigate excessive risk-taking practices' (G20, 2009a:8). In order to persuade members of the efficacy of such an approach however, the IMF provided justification for doing so based on two premises.

Firstly, although advocated during the first phase, substantial weaknesses in the Basel 2 rules for regulating commercial banks were increasingly apparent. A key problem was that as late as September 2007 the GFSR (2007a:1) had suggested that 'systemically important financial institutions had began this episode with more than adequate capital to absorb the likely level of credit losses', yet it became quickly evident that this was clearly not the case. This situation was exacerbated by the fact that banks were unable to sell assets in a down-turn to cover their losses was mistaken, with some not even being able to sell at a loss.

In hindsight there was therefore a sense that much responsibility had been deferred to the market (even during the first phase of the turbulence), yet as 2008 progressed, such was its severity, Basel 2 would not be sufficient to prevent a similar collapse should regulatory inadequacies persist and that more substantive action was required (Vinals et al, 2010:6).

Secondly was an assertion that MicPR was necessary but not sufficient to deal with systemic risk. Although Basel 1 and 2 operated on the notion that ensuring the solvency of individual institutions would lead to resilience in the broader system, the banking and financial sector collapse highlighted that: problems associated with particular institutions have destabilising systemic implications; aggregate risk is premised on the collective, not individual behaviour of financial institutions which can create undesirable outcomes for the system as a whole; and making individual institutions safe does not guarantee systemic stability.

Strauss-Kahn (2009b:4) suggested that this MicPR approach reflected the propensity of supervisors which was to gaze inwards, focusing on the health of domestic institutions and protecting domestic consumers. That the collapse had demonstrated a need to focus more on global systemic risks however provided the rationale for a shift in emphasis from an exclusively micro-, to a complementary micro-/macro-prudential approach to regulation.

The preceding discussion suggests that, in contrast to the neoliberal economic philosophy, just as there appeared to have been a recognisable shift observed in Chapter 4, so too here was there an apparent collective recognition of the need for decisive intervention to rid banking and financial sectors of their accumulated pathologies to bring about substantive change. In doing so, there appeared to exist the potential for a similar shift to a distinctive political economy calling on the power and resources of the state to bring about economic stability and prevent a future banking and financial sector collapse of a similar magnitude.

Policy implications

During the second phase of the downturn, the key problem so-defined shifted substantially from supervisory to regulatory failings. In doing so, calls for a new rules-based approach opened space for more substantive government intervention into financial markets. Indeed, by becoming the principal interpretive frame through which the problem was defined, global economic governance institutions tasked with responding to the collapse including the IMF, FSB and BIS were presented with an opportunity to instantiate substantial reforms.

The shift in problem definition therefore constituted more than the provision of an alternative way in which the problem was 'framed', since, because the cognitive filter had been seemingly switched to an altogether different setting, a range of potential policies considered out of reach prior to the downturn suddenly found themselves on the table.

These included countercyclical capital requirements; countercyclical liquidity requirements; caps on aggregate lending; reserve requirements; limits on leverage in asset purchases; loan to income ratios for mortgages; transaction taxes; additional loss absorbency related to systemic importance (IMF/FSB/BIS, 2011:11). Nevertheless, it was suggested by the G20 (2009a:6) that although reforms must be multi-faceted 'at its core must be stronger capital standards' which 'allows banks to withstand the losses that inevitably will come'.

It is here attention once again turned to the Basel accords, yet rather than suggesting the need to supervise the implementation of Basel 2, the IMF, FSB and BIS sought the provision of a new set of rules (Basel 3) to better reflect the changed realities presented by banking and financial sector turbulence. Crucially not only were states persuaded of the efficacy of Basel 3 in cognitive terms (given the falsification of the economic ideas underpinning the neoliberal economic philosophy) but also normatively in respect that regardless of the global scope of financial activity, it fell on national tax-payers to fund financial rescues which carried with them enormous distributional consequences. The magnitude of the contextual trigger therefore exacerbated calls for the kinds of reforms unthinkable only months prior.

In doing so, Basel 3, just as Basel 2 had done, incorporated major amendments to alleviate the shortcomings of its predecessor through 'the conscious need to complement the micro-level of financial supervision with the macro-prudential dimensions', which constituted 'a fundamental turning point in the design of financial regulation' (Caruana, 2010:3). In particular, the IMF (Perotti et al, 2011; GFSR, 2010) stressed the need for more stringent capital requirements and for banks to hold excess capital as conservation and counter-cyclical buffers above the minimum to complement traditional moral suasion and targets used by regulators, along with a leverage ratio to offset deficiencies in risk-weights.

Both MicPR and MacPR approaches would welcome this development as both perspectives encourage the build up of capital and liquidity buffers in the upward phase of the cycle when there are signs that individual institutions may be increasing leverage and relaxing underwriting standards and when systemic risk is rising. However, though directionally policymakers are likely to agree, differences arise over the timing and scale of the build up of buffers. In practical terms, the micro-prudential authority will scrutinise individual firms' credit standards and provisioning, and will intervene through Pillar 2 mechanisms. The macro-prudential authority on the other hand will monitor, and act on, indicators that will trigger the use of countercyclical buffers or other tools that affect credit granting.

Differences between the two approaches, while potentially negligible during the early stages of the up-swing, may start diverging when the cycle approaches its peak. At this stage MicPR indicators appear very positive, while systemic risk indicators give increasingly urgent warning signs. This has been referred to as the paradox of financial instability – the system appears strongest precisely when it can be most vulnerable as what looks like a low risk environment is in fact a reflection of aggregate risk taking (Osinski et al, 2013:13).

Reflecting this assumption, although not a new minimum capital requirement, Basel 3 suggests that outside periods of stress, banks should hold buffers of capital (a conservation buffer) above the regulatory minimum, funded by reducing the discretionary distribution of earnings such as by reducing dividends, or by raising capital from the private sector (BCBS, 2010:54). The overall aim is to ensure that banks are in such a position as to conduct business as normal when their capital levels fall as they experience losses during downturns.

Operating on the assumption however that initiatives to improve existing bank regulations by building up larger individual buffers to withstand shocks, this did not address a key lesson - that it was a global systemic event in which institutions were connected through markets and instruments. Basel 3 therefore calls for the deployment of additional counter-cyclical buffers to ensure capital requirements take account of the macro-financial environment.

The suggested aim is to deploy these buffers when excess aggregate credit growth is judged to be associated with a build-up of systemic risk to ensure the banking system has a buffer of capital to protect it against potential losses. This would be assessed against credit growth (i.e. is it excessive?) and would: extend the size of the capital conservation buffer; consist of CET1 assets; and be phased in, reaching 2.5 percent by 1st January 2019 (BCBS, 2010:57-60).

The counter-cyclical capital buffer in Basel 3 was therefore designed to accumulate capital in boom times when systemic risk builds up so that it can be used when such risks materialise, thereby acting as a stabiliser during the expansion and contraction phases of the financial cycle. Adjudicating the right time to deploy the buffer requires that national authorities monitor credit growth and other indicators that may signal a build-up of system-wide risk. Based on this assessment, the countercyclical capital buffer will be deployed, thereby extending the capital conservation buffer, with banks being subject to restrictions on capital distributions if they do not meet the additional capital requirement (IMF/FSB/BIS, 2011:13).

This would mediate for the fact that once the cycle turns, the aim of MicPR is to ensure the stability of individual firms, while MacPR is concerned with stabilising the broader system and avoiding excessive deleveraging pressures that can lead to, or exacerbate, a downturn. A MacPR approach would therefore be wary of potential collective contraction and undue pressure on asset prices which would weaken growth and undermine the systems resilience. So, it would advocate the release of capital buffers built up earlier as prevailing levels should allow for this without jeopardising confidence. Indeed, the higher the buffers initially, the greater the policy space for drawing on them earlier and faster (Osinski et al, 2013:14).

The incorporation of a counter-cyclical buffer had previously been off the table. Its incorporation in Basel 3 however, seemingly re-empowered regulators by providing a basic rationale for increased state intervention to curb and place limits on financial excesses. As a result, it was retrospectively described by Kodres and Claessens (2014:8) as a first international attempt to institute an effective macro-prudential tool.

The preceding reforms to international regulation and the policies advocated as part of this new agreement rejected the previous policy consensus centred upon disclosure, the need for better information, and market discipline. Indeed, 'they primarily suggest reducing the scope of private-sector self-regulation, and enlarging the scope of financial regulation', which signalled 'important discontinuities with the policy ideas that had previously been at the heart of the international financial system' (Moschella, 2010:145).

Indeed, at this juncture there was an assumption, exemplified by Strauss-Kahn (2009d:1) that 'this terrible crisis has... provided us with an historic opportunity to reshape the global economic and financial framework – and thus lay the foundations for strong and sustainable economic growth going forward'. Indeed, just as Chapter 4 observed that IMF staff, drawing on the lessons learned from history, referenced the Great Depression as a moment of economic uncertainty that ultimately gave rise to altered economic structures, so too was it invoked in this instance. Strauss-Kahn (2009d:1) for example noted that just as the Great Depression and World War Two helped to shape a new global order, so too did leaders have a similar opportunity 'to emerge from the financial crisis and achieve fundamental and lasting change'. Of this opportunity Strauss-Kahn (2010d:2) suggest that the shift to Basel 3 constituted 'a major step in the right direction' towards a safer financial system.

This sense of achievement was echoed in the G20 Toronto Summit Declaration which noted that 'the amount of capital will be significantly higher and the quality of capital will be significantly higher and the quality of capital significantly improved when the new reforms are fully implemented. This would enable banks to withstand – without extraordinary government support – stresses of a magnitude associated with the recent financial crisis' (G20, 2010:4). Indeed, Hannoun (2010:1), Deputy General Manager of BIS noted that Basel 3, fully implemented, 'will have considerably reduced the probability and severity of a crisis in the banking sector, and by extension, enhanced global financial stability'.

The preceding discussion demonstrates the importance that defining the prevailing political-economic problem as one of regulatory as opposed to supervisory failure had for the kinds of policies that were subsequently considered necessary. Indeed, that policies that appeared to diverge substantially from those associated with extant economic ideas were so rapidly deployed in the context of failure was consistent with constructivist approaches that highlight that such moments open windows of opportunity with which to effect change.

Implications for the neoliberal economic philosophy

Schmidt (2011:2-3) has noted that, as a rule, policy priorities are those which change most rapidly as windows of opportunity open up through which to enact change. Nevertheless, economic philosophies are typically confined to the normative, as opposed to the cognitive, sphere, a reflection of ideas regarding the appropriate role of states or markets. That these are inherently political means they are often held up as being those that are most resistant to change.

This notwithstanding, the kinds of policies advocated by the IMF during the second phase of the downturn appeared to carry with them important implications for the neoliberal economic philosophy, that is, the perceived efficacy of markets as opposed to states. As a result, the second phase seemingly did more than simply open a window of opportunity in which to push for the enactment of policies that might be better placed to address the immediate problems facing policymakers. Rather, they appeared, superficially at least, to serve as a potential pre-cursor to a fundamental transformation in the economic ideas steering IMF policy priorities.

At its Washington summit, leaders noted that 'the IMF, with its focus on surveillance, and the expanded FSF, with its focus on standard setting, should strengthen their collaboration, enhancing efforts to better integrate regulatory and supervisory responses into the macro-prudential policy framework' (G20, 2008:10). This was premised on the fact that because MicPR focuses on the responses of banks to exogenous risks this neglects endogenous risk. MacPR however acknowledges that the global financial system is now so complex that what is suitable for individual institutions may have destabilising consequences for the broader system. Although recognising the health of individual financial institutions is a necessary but insufficient condition for financial stability, Osinski et al (2013:5) of the MCMD note that MacPR, by alerting relevant authorities and pushing for action, is better placed to capture systemic risk.

A joint IMF/FSB/BIS Progress report to the G20 highlighted agreement among three defining elements of a MacPR approach. Firstly, its objective is to limit systemic risk, the failure to do which was laid bare by the banking sector collapse. Secondly, its scope is the focus on the financial system as a whole as opposed to the individual components that take the broader system as given. Finally, its instruments are primarily prudential tools calibrated to target the source of systemic risk (IMF/FSB/BIS, 2011:4; IMF/FSB/BIS, 2011a:2).

The ultimate objective of MacPR is therefore to avoid the kind of output and wealth losses generated by the financial and economic downturn. The rationale for doing so is that during the up phase of a cycle, as asset prices rise, measured risk appears to fall. In contrast, when asset prices fall, risk appears to rise, asset sales commence, views on acceptable levels of debt are revised downwards, uncertainty prevails, and credit contracts (Baker, 2012:114).

In order to limit the build-up of system-wide financial risk, a MacPR approach, by addressing negative externalities, acts as a countervailing force to the decline in measured risks in a boom and rise in a downturn. Indeed banking and financial sector pathologies highlighted the need to counter the pro-cyclicality of financial markets by implementing counter-cyclical regulatory policies to induce institutions to build up capital buffers in good times so they could be drawn down in bad times to stabilise the worst excesses of pro-cyclicality. Doing so, it was thought, would contribute to a more stable institutional environment.

With the preceding discussion in mind, Baker (2013:116) noted that the coordinative discourse centring on the need for a complementary MicPR/MacPR approach constituted a 'startlingly rapid ideational shift', that is, a radical change in the overarching terms of policy discourse inasmuch as it: run contrary to the identifiable material interests of the major players and had therefore been on the side-lines previously; and was undertaken within an incredibly short time-frame.

A MacPR approach therefore seemingly challenged the existing neoliberal economic philosophy and the analytical foundations of the efficient market orthodoxy that had dominated, through what Tsingou (2010:27) referred to as the re-politicization of financial regulatory policy. That is, it advanced an altogether different conception of market relations than that of the neoliberal economic philosophy by increasing the power of public authorities to intervene and set limits to financial market activities, particularly those considered potentially socially damaging.

MacPR was therefore presented as a series of new premises that refuted the old Basel consensus of transparency, disclosure, and risk management as the foundation for efficient markets. Most notably, because MacPR considers financial instability endemic and endogenous to the system, it has been shown to: create space for more extensive interventions (a reassertion of public authority over private interest); and adopt a normative stance that regulation should be less costly to society than to the private sector.

This shift therefore implied a return to regulators telling banks what they should do as opposed to asking them what it is that they do, a move which involves a ‘reconstitution of power relations at the heart of financialised capitalism' (Baker, 2013:7). In this respect, the shift to a complementary MicPR/MacPR approach to regulation was interpreted by its proponents as ‘a substantial intellectual sea-change in the thinking driving international financial governance’ (Baker & Carey, 2014:100) which had ‘switched the principal cognitive filter employed by policymakers to an entirely different setting’ (Baker, 2013:7, 19).

The shift from the banking and financial turbulence (the first phase) to economic downturn (the second phase) therefore seemingly had important implications for the manner in which the relative efficacy of states and markets were once again understood in the IMF as the moment of failure was seemingly crucial in having all of the components necessary to impose a new trajectory upon the state (Hay, 1999:317). That is, the notion of the valorised financial markets portrayed as natural and self-regulating, once again oscillated back to the recognised need for intervention in which sates would assume a more prominent role in limiting the market excesses associated with banking and financial sector activity.

Such a shift both: suggests that the economic ideas through which the turbulence was interpreted during its first phase was abandoned in the face of evidence which contradicted existing cognitive and normative assumptions regarding the relative efficacy/desirability of markets and states; and consequently draws attention to the fact that the economic ideas steering the course of global economic governance have the potential to be created and recreated through the action of political actors in the context of failure as actors’ ideas and discourse about their prior beliefs alter in response to changed performance/circumstances.

Accepting the notion that the ‘common sense’ assumptions, in this instance those held by the IMF and others constituting the coordinative discourse regarding the efficacy of free markets, prevail only during a given era, and suggests that they be best understood as 'ubiquitous aspects of social coordination' (Bevir&Trentmann, 2002:21). This highlights the diversity of possible forms of economic ideas which in this instance was characterised by a consensus regarding the need for a complementary MicPR/MacPR approach that appeared better placed to address pressing problems.

Taken together therefore, during the second phase, the IMF appeared, superficially at least, to be characterised by a large degree of change as opposed to continuity. That is, faced with the inefficacy of the prevailing regulatory framework to sufficiently prevent banking and financial sector pathologies, the IMF called for major change to the regulatory architecture. This shift was shown to have important implications not only for the policy realm but more pertinently, for the neoliberal economic philosophy and the manner in which the relative efficacy of states and markets were once again understood.

This demonstrates how the kind of economic ideas advocated in the coordinative discourse and justified through research developed in the communicative discourse exist only in a particular time and space, embodying particular values, and interests. Indeed, despite becoming embedded within institutional contexts, sometimes coming to constitute the common sense of a particular era as the efficacy of freely functioning and self-regulating markets had done, these claims were shown to be contingent and incomplete.

Concluding remarks

Two key points can be derived from the preceding discussion. Firstly, during its initial phase, the effects of banking and financial pathologies were only minimal as the IMF interpreted the problem as one of supervisory inadequacies. It was therefore suggested that all that was required to bring stability to the system was the increased provision of information, enhanced disclosure, and the supervision of the full implementation of Basel 2. As a result, during the first phase, neoliberal economic ideas continued to shape how problems were interpreted and responded to, and set the parameters of the acceptable policy response.

Secondly, as banking and financial sector pathologies began to implicate the real economy it was evident that many of the assumptions on which neoliberal economic ideas were constructed were fundamentally flawed, including belief in the ability of financial markets to self-regulate and tend towards equilibrium. With the banking and financial sector collapse being interpreted as a more fundamental failure of regulation, the IMF advocated the shift to Basel 3 which accorded states considerable scope to intervene in financial markets to prevent the most severe excesses of banking and financial market activity. Consequently, as the second phase unravelled there appeared something of a consensus that the collapse would prove to be a re-constitutive event for the neoliberal economic ideas steering IMF policy priorities.

This ostensible shift notwithstanding, Chapter 7 suggests that the banking and financial sector collapse has not imbued in the IMF a radical change in the manner in which the relative efficacy of states and markets are understood. Rather, Chapter 7 demonstrates that the IMF continues to exhibit a considerable degree of stasis in the manner in which economic problems are interpreted and responded to, and thereby, the kinds of policies considered necessary.

Chapter 7

Financial sector liberalization II

'Those who cannot change their minds cannot change anything'
(George Bernard Shaw)

Introduction

The previous chapter made two claims. Firstly, that in its first phase, the IMF interpreted banking and financial sector pathologies as a problem of supervisory failure, and therefore resolvable with policies derived from existing frames of reference. Secondly, as the down-turn entered its second phase the IMF appeared to be characterised by a considerable degree of change as the core problem facing policymakers shifted from supervisory to much more fundamental regulatory failures. Indeed, this 'startlingly rapid ideational shift' (Baker, 2012:3) created space for substantive state interventions into the functioning of markets through the enactment of policies previously considered off the table prior to the downturn.

This notwithstanding, this chapter argues that, as the third stage (a shift in focus towards sovereign debt sustainability) progressed, it became evident that the downturn had not imbued major change in the IMF either in its adherence to the neoliberal economic philosophy, problem definitions or policy priorities. Rather, it is suggested here that the IMF, along with other institutions constituting the coordinative discourse, never abandoned their normative deference to neoliberal economic ideas, despite assertions to the contrary during the second phase.

As a result, although there appeared to be a clear direction, rationale, and commitment to, reform, it was increasingly being talked of as something for the future. Reflecting this impasse, Kodres and Narain (2010:4) suggested two potential regulatory scenarios: (1) having skirted economic collapse, and facing strong resistance from the private sector to new regulation, the official community allows complacency to set in and reform is allowed to languish; and (2) the crisis has been so devastating that every public body wants to be seen as responding vigorously which could lead to over-regulation. This chapter demonstrates how it is the former of these scenarios that has played out.

Phase 3: Problem definition

The IMF was not an institution that supported, or acknowledged an over-whelming necessity, to aggressively regulate the banking sector despite the severity of the afflictions presented by its pathologies. Rather, it remained an institution that exhibited a considerable degree of caution in the regulatory reform debate. As a result, although the IMF consistently espoused the benefits of Basel 3 (GFSR, 2012), as the third phase of the downturn progressed through the course of 2010, this commitment was increasingly couched in a broader context in which it cautioned against the potential for too-stringent capital adequacy reforms.

The majority of this research came after the basic Basel 3 reforms had been agreed, yet before the fine details of its composition had been finalised, and before the implementation phase. There was however, no suggestion that the IMF was attempting to argue for a fundamental re-shaping of the regulatory reform agenda. What drawing attention to this research does do however is provide us with both an important insight into the extent to which the IMF remained sceptical about the potential efficacy of reforms. Moreover, it elucidates the manner in which the IMF approached the initial reform agenda.

Doing so allows us to highlight, crucially, how the intellectual parameters for reform were inherently constrained by the IMF, and other institutions constituting the coordinative discourse's continuing deference to the neoliberal economic philosophy. Doing so is consistent with the constructivist principle that the need to reform the existing Basel accords, and the form that this might take, was not dictated by the nature of events, but was informed through interpretive processes which were themselves guided by the broader context of, in this particular instance, the neoliberal discourse.

This helped to focus the attention of the IMF, and others, by specifying what was relevant or otherwise in the reform agenda, the result being that only one particular set of meanings or problem definitions acquired relevance over the range of alternative pathways that were invariably available at this juncture (Benford, 1997:410). We therefore show how the manner in which reforms were construed, and constructed, by the IMF and others was 'an inherently political process' in which an attempt was made to frame the kinds of policies considered necessary (Blyth, 2012:8). This reminds us that meanings do not naturally attach themselves to events, but rather arise through interactively-based interpretive processes (Snow, 2004:384).

That the IMF and other institutions of the coordinative discourse sought to frame and set normative limits to the parameters of what could and could not be subject to deliberation was a clear expression of power. However, this power was not simply manifest in terms of the IMFs capacity to impose its will on others, but more importantly, in its authority to determine the shared meanings that set the terms of the regulatory reform debate. That is, it included 'the ability to create the underlying rules of the game, to define what constitutes acceptable play, and to be able to get others to commit to those rules' which was a more subtle and effective expression of power (Adler, 1997:336).

The consequences of limiting the reform agenda within the normative parameters of the neoliberal discourse however was that as 2010 progressed and the economic environment was increasingly benign, practitioners and market actors sought to exploit space - in which after the most acute phase of the downturn was over, with reforms incomplete, and with underlying causes remaining insufficiently addressed - in which to draw back from the exceptional measures advocated during the second phase. Indeed, Strauss-Kahn (2010c:1) suggested that 'as a single major challenge gives way... the policy responses might be less obvious, and the common sense of purpose weakening'.

The desire for reform therefore appeared to wane as perceived benefits became distant memories, and the rationale less urgent as the most acute phase of the downturn faded into the background, replaced as it was by a seemingly more pressing problem, sovereign debt excesses. This was a scenario observable in the IMF where reference to capital regulatory reform for example had largely disappeared from the "headline" publications (WEO and GFSR) by 2010 with reforms increasingly talked of as something for the future (Kodres & Narain, 2010:8).

Indeed, against the backdrop of an increasingly benign economic environment and a re-framing of the prevailing economic problem (sovereign debt excesses), the IMF shifted its focus (albeit much more subtly than that observed in Chapter 5) from calls for substantive regulatory reform, to instead providing the cognitive justification for a more cautionary approach to regulation broadly construed, and of capital adequacy in particular.

The Modigiani and Miller theory (1958) suggests that, under ideal conditions, adding equity capital does not increase costs as, under specific conditions including perfect markets and no distortions introduced by government policy, the proportion of a firm's funding coming from equity is immaterial to its weighted average cost of funds as investors in equity and debt do not charge as much for supplying funds to a safe, as compared to a less safe, company. That is, investors accept a lower expected return in exchange for the reduced risk and volatility resulting from higher capital levels and lower probability of default.

In practice however, higher equity levels do increase a bank's costs, with two distortions in particular created by public policy interfering with the offsetting mechanism. First, virtually all governments provide a tax advantage to debt issuance by allowing corporate deductions for interest payments, but not for dividends. Secondly, there are a host of explicit/implicit guarantees of bank liabilities. When deposits are guaranteed by governments for instance, deposit rates will be insensitive to the relative safety of the bank. Increased equity will not create a major offsetting decrease in the rate required by depositors (Elliott et al, 2012:28).

This discussion captures effectively the crux of the contemporary capital adequacy debate in the IMF. That is, although it is acknowledged that higher capital requirements reduce the risk of bank bankruptcies and lower leverage, requiring banks hold more and better capital is not cost neutral and these costs must be borne somewhere. This tension was highlighted in an MCMD paper which noted that although 'reforming the regulation of financial institutions and markets is critically important and should provide large benefits to society... adding safety margins in the financial system comes at a price' (Oliveira & Elliott, 2012:4). This shows how the desirability of increased capital was not universally accepted but was in fact hotly debated.

The research produced by the IMF did not argue against the benefits of capital buffers per se. Indeed, it was acknowledging of the fact that if capital requirements are mild, a bank subject to regulation invests more in lending and its probability of default is reduced. What it did do however was essentially act as a cautionary warning against too-stringent capital buffers, whose consequences, unintended or otherwise, according to De Nicolo et al (2012:3) have the potential to negate efficacy and welfare benefits which disappear and turn into costs.

Against this backdrop, an attempt was made to quantify the potential problems associated with reforms that went too far beyond what would be desirable. Indeed, despite the fact that the negative effects of the market-based approach to regulation were seemingly interpreted as a major precipitating cause of the downturn, which in its self demonstrated that regulatory reforms of the banking sector were potentially beneficial, Blanchard

(2009:6) typified the assumption in the IMF that reforms should proceed, 'without hindering too much its efficiency'.

Similarly when deciding on when and to what extent to act Arregui et al (2013:7-8) observed that policymakers need to compare the possible benefits of avoiding/reducing the depth of a downturn with the costs of tightening intermediation in the present. That is, they need to consider the imperfect nature of the signal and the possibility of over-regulation (in this case through capital buffers), as they could act on a signal that is false in the first place (a "false positive"). Given that the ultimate objective of policy should be to bolster long-term real economic activity when considered against blows arising from financial crises, this is where the discussion regarding cost and benefits is played out, and which inform future decisions.

For its part, while acknowledging the potential efficacy of non-too-stringent regulation, IMF research, derived predominately from the MCMD drew attention to the importance of caution in the capital adequacy debate. It is presented hereon in as follows: increases in the cost, and reduced volume of, loans; divesting business activity; reduced GDP growth; and tail risk implications.

Increasing cost of loans and decreasing demand for loans

Banks exercise some control over the spread of their marginal lending and deposit rates with respect to the central bank policy rate. The spread between deposit and lending rates allow banks to make profits, part of which is distributed to shareholders, with the remaining profits used to cover operating costs and to accumulate capital buffers. The introduction of regulatory reforms calling for banks to raise their capital buffers will therefore, according to Oliveira and Elliott (2012:9) change the variables that make up the loan pricing formula, forcing banks to make offsetting adjustments to one or more, ultimately increasing costs.

In assessing the likely impact of the new capital requirements introduced under Basel 3 on bank lending rates and loan growth, Cosimano and Hakura (2011:2-12) infer the impact of an increase in capital regulations on the loan rate charged by the largest banks. In doing so, they find that a 1 percent increase in the equity-to-asset ratio is associated with a 0.12 percent increase in the loan rate for the one hundred largest banks. For banks in countries that experienced a banking crisis during 2007-9, it is associated with a 0.09 percent increase in the loan rate; and a 0.13 percent increase for those that did not. Thus, under normal conditions, the projected 1.3 percent increase in the equity-to-asset ratio required for banks under Basel 3 would increase the loan rate by 16 basis points for the 100 largest banks.

These findings were broadly replicated by Elliott et al (2012:68) who noted that capital buffers come with additional costs, typically borne out by increases in the lending spread. In particular, the authors suggest that higher operating costs will be passed on to consumers which - given divergent national implementation strategies – will see lending rates likely rise by about 17 basis points for Europe, 8 basis points in Japan, and 26 basis points the US, with Roger and Vlcek (2011:13-14) observing even higher peak rises on lending spreads: 120 basis points in the Euro area and 130 basis points in the United States.

The corollary of credit price increases would, it has been suggested, be a downward demand for loans. Cosimano and Hakura (2011:5-18) for example, imply a 1.3 percent increase (5.7% to 7%) in the equity-to-asset ratio required by Basel 3 would reduce loans for the 100 largest banks by 1.3 percent. Moreover a declaration of "excessive credit growth" requiring an additional 2.5 percent increase in the equity-to-asset ratio was predicted to reduce loans by 2.5 percent in the long run. Assuming a 1.3 percent increase in the equity-to-asset ratio to meet Basel 3 regulations, estimates imply a reduction in the volume of loans by 4.6 percent in banks in countries that experienced a crisis and 14.8 percent in countries that did not.

Under the scenario envisaged above, too stringent capital requirements and declining demand for loans were shown to have the potential to push banks to divest themselves of noncore business. Indeed, it was suggested that even without additional regulation, the higher cost environment and difficulty of managing complex institutions may induce banks to divest business lines to improve profitability by becoming more specialised. Indeed, as early as 2010 Kodres and Narain (2010) noted that many were already doing just this.

This had the potential however to lead to an even further concentration of certain activities in the largest banks as smaller banks, particularly those operating in the commodities and currencies markets reduce their market share given reduced profitability. This, it was thought, would further contribute to the problem presented by too big to fail banks.

Implications of capital adequacy for GDP growth

The increase in lending spreads and associated reduction in the volume of loans, along with a concentration/re-focusing of core business activities had the potential to induce a slowing of consumption and investment. Adequately deployed however, Roger and Vitek (2012:3-9) suggest that monetary policy responses would typically reduce the adverse impact of higher capital requirements. The option for this instrument however, was heavily constrained, at least over part of the implementation period. The potential for a slow-down in consumption and investment therefore increased, although research differed greatly in its estimates.

Arguably the most comprehensive study into the cost impact of capital adequacy reforms on GDP was that undertaken by the Institute of International Finance (IIF, 2011), an association representing over 400 financial institutions globally. The study predicts significant increases in the price of credit, the result of which was that GDP in major economies was estimated to be about 3 percent smaller in 2015 than it would be in the absence of regulatory reforms.

Elliott et al (2012) however suggest that the IIF study demonstrates a far larger cost to financial reform measures than seems plausible, particularly given it is primarily concerned with transition effects in the short- to medium-term. Research conducted by Elliott et al (2012) however analysed the long-term effects of capital buffers. In doing so results showed that higher capital requirements while impacting hard on all forms of banks, the effects on GDP growth, while still consequential, were lower than that conceived in the IIF study.

Roger and Vitek (2012:3) on the other hand analysed the transitional costs of strengthening bank capital requirements with specific emphasis on globally systemically important banks (GSIBS) and with analysis focusing solely on the short- to medium-term output costs of the proposed measures. In doing so, the authors estimated that a synchronised global increase in capital requirements for all banks by 1 percent would cause a peak reduction in GDP of around 0.5 percent, of which, around 0.1 percent would result from international spill-over's with losses in emerging economies being even higher than in advanced economies.

Should banks elect to cut risk-weighted assets (RWAs) in order to raise capital ratios instead of increasing the costs of loans however the impact on GDP growth, it was suggested, would be even greater. This is a strategy most likely to be undertaken through a gradual reduction in target loan-to-value (LTV) ratios and would be followed if banks had very little time in which to adjust capital ratios, since this would give little time to build up capital through dividend cuts or widening of lending margins. The cut in bank lending envisaged under this strategy leads to sharp contractions in investment and consumption as adverse demand effects are amplified as weaker spending leads to declines in asset values, cutting collateral values and access to credit. As a result, economies were predicted to experience peak contractions in real economic activity relative to potential of around 1.3 percent (Roger & Vlcek, 2011:12-15).

Tail risk considerations

Historically, tail risk in traditional loan-oriented depository banking was low (both project returns and withdrawals largely satisfied the law of large numbers), hence “skin in the game” effects dominated, and extra capital led to lower risk-taking. In the contemporary financial system however, when banks have access to tail risk projects, traditional buffer and “skin in the game” effects become weak, while effects where higher capital enables risk-taking became stronger. Therefore, due to financial innovation, the beneficial effects of higher capital are reduced while the scope for undesirable effects is increased.

Underpinned by this assumption, Perotti et al (2011:3-4) reviewed the effectiveness of capital regulation, and in particular of excess capital buffers in dealing with tail risk events. In doing so, two key observations were made. Firstly, traditional buffer effects of capital are less powerful when banks have access to tail risk projects, the reason being that tail risk realizations can wipe out almost any level of capital, so limiting the effectiveness of capital as an absorbing buffer. Secondly “skin in the game” is restricted because part of the loss is never borne by shareholders. Hence, under tail risk, excess risk-shifting incentives of bank shareholders may exist almost independently of the level of initial or required capital.

Elliott et al (2012) similarly highlight that banks are increasingly exposed to tail risk, which causes losses only rarely, but when those materialise they often exceed any plausible initial capital due to the following strategies: firstly, carry trades reliant on short term wholesale funding produce highly correlated distressed sales; secondly, the reckless underwriting of contingent liabilities on systemic risk were callable at times of collective distress.

Taken together, since under tail risk banks do not internalise losses independently of the level of initial capital, the buffer and incentive effects of capital diminish, with higher capital in fact becoming a less effective way of controlling bank risk in the contemporary banking system. This is a point exemplified by the collapse which demonstrated that a number of major banks suffering severe adverse shocks had appeared sufficiently capitalised prior.

Secondly, having established that under tail risk the benefits of higher capital are limited, Perotti et al (2011) consider its unintended effects. In doing so, the authors note that capital regulation affects bank risks choices through the threat of capital adjustment costs when banks have to raise equity to comply with minimum capital ratios. Similar to "skin in the game" capital adjustment costs fall with higher bank capital because the probability of breaching capital ratios decreases. Indeed if highly capitalised banks internalised all losses, they would take risk only if that was socially optimal. This changes as tail risk is introduced as then, even banks with high capital never internalise all losses and may take excess risk.

Research therefore demonstrated that tail risk can lead to insolvency whatever the initial bank capital, so, higher capital does not discourage risk-taking even for well capitalised banks. At the same time, excess capital allows banks to take on risk without breaching the minimum capital ratios in the case of low (non tail) returns. So under tail risks, higher capital may create conditions where highly capitalised banks actually take on excessive risks.

Demirguc-Kunt et al, (2010:3) similarly suggest that when capital is low relative to the regulatory minimum banks choose a risky loan portfolio to maximise the option value of deposit insurance. As capital increases and future solvency becomes less likely, on the other hand, incentives to take on risks are curbed by the desire to preserve the bank's charter value. However, when banks become so well capitalised that insolvency is remote, an additional increase in capital induces banks to take on more risk to benefit from the upside.

Perotti et al (2011) therefore suggest that it is impossible to control all aspects of risk-taking using a single instrument, the problem of capital buffers being that they are effective as long as they can minimise the chance of default, and the loss given default. However, innovation in finance allows intermediaries to manufacture risk profiles which let them take advantage of limited liability even with high levels of capital. The key to contain gambles with skewed returns, it was therefore noted, was to prohibit extreme bets or increase their ex ante costs.

Implications

The up-shot of this research was not that less capital is better: banking and financial sector pathologies, along with their subsequent impact on economic growth, clearly demonstrated that this is not the case. Nevertheless, the following conclusions can be drawn. Firstly, its aim was to communicate the point that traditional capital regulation has limitations. And secondly, banks with significant excess capital may be induced to take excessive risk (to use or put at risk their capital), as aptly demonstrated by the downturn. Therefore, relying on higher and excess capital to prevent future financial crises could have ruinous effects.

This research cautioning against too-stringent capital adequacy regulation provides us with a strong sense of how the IMF continued to be guided by neoliberal economic ideas, the economic philosophy of which carried with it explicit assumptions regarding the negative consequences associated with government interference into the functioning of financial markets. Indeed, this assumption played a crucial part in influencing the debate on banking and financial sector regulation and provided the justification for a largely hands-off approach to regulatory policy.

Indeed, we can see again in this instance how, despite now acknowledging the need to provide some semblance of regulation, these assumptions made prior to the downturn were increasingly manifest in the capital adequacy debate. That is, just as IMF staff had seemingly been at the fore-front in calling for greater regulation, so too did they now find themselves helping to provide acceptable narratives of the third phase of the downturn, calling for caution in the capital adequacy debate. Implicit here was a continuing distrust, and potentially negative consequences associated with, government intervention, along with a continuing belief in the efficacy of freely-functioning markets.

This research can therefore be read as an attempt to ensure that the frames through which regulatory standards had been perceived prior to the down-turn were not completely over-hauled. This process was certainly made easier inasmuch as, although not impregnable, having become firmly entrenched as ‘institutional fact’ (Searle, 1995) in the IMF in the period preceding the downturn as belief in the ability of managers to manage their own risk portfolios had done, substantive change was, in many respects, largely precluded by continuing adherence to extant economic orthodoxy.

The kinds of arguments raised in IMF research were however, by no means uncontested. Indeed, one of the biggest critics, Admati, outright rejected the cognitive assumption that larger capital buffers are correlated with an increased cost of loans. This had obvious knock-on effects for research regards the decreasing number of loans and the impact on GDP.

The starting point for criticism was a key argument in IMF research that 'a pervasive view that underlies most discussions of capital regulation is that "equity is expensive", and that equity requirements, while offering substantial benefits in preventing crises, also impose costs on the financial system and possibly on the economy' (Admati et al, 2013:i).

This, the authors suggest, is troubling as the view that equity is expensive is flawed in the context of capital regulation. On the one hand, Admati et al (2013:3) suggest that higher equity capital requirements need not affect the lending activities of banks since highly leveraged banks are subject to distortions in their lending decisions, while better capitalised banks are likely to make better lending decisions. In particular, they will have less incentive to take on excessive risks and will be subject to fewer problems related to "debt overhang" that can actually prevent them from making valuable loans. As a result, 'there is no reason to believe that, if overall public policy forces banks to operate with significantly higher and safer equity levels and if any subsidies are set in a socially responsible way, banks would refrain from making loans that would lead to growth and prosperity' (Admati et al, 2013:3).

On the other hand however, the authors suggest that increasing equity requirements need not interfere with any of the socially valuable activities of banks including lending, deposit taking, or the creation of "money-like", liquid, and "informationally-insensitive" securities that might be useful in transactions. In fact, they suggest that the ability to provide social value would generally be enhanced by increased equity requirements because banks would be likely to make more economically appropriate decisions. By not requiring more stringent capital requirements however, there was every chance that banks will be free to once again engage in risky activity, knowing that they will be bailed out in the event of a downturn.

Finally the authors noted that, from a normative perspective, the downturn showed that having a fragile financial system in which banks and other financial institutions are funded with too little equity is inefficient and incredibly expensive from an economic and political perspective. Contrastingly however, the authors suggest that the social costs of significantly increasing equity requirements are, if there are any at all, very small. All arguments to the contrary are therefore deemed by Admati et al (2013:i) as being 'very weak' and premised on 'fallacious claims', based on inadequate theoretical models and empirical evidence.

That this is the case once again draws attention to the fact that research undertaken by the IMF was driven as much by political suasion, a reflection of a continuing commitment to the normative ideas underlying the neoliberal economic philosophy as it was by any other means.

This supports the assumption made in Chapter 1 that research is a key method by which the IMF attempts to shape economic knowledge and ensure congruence with dominant economic ideas by providing cognitive justification for particular economic philosophies and problem definitions. In doing so, in this instance, an attempt was made by the IMF to shape the context in which actors found themselves and pursued their preferences by dictating that action was directed to the selection of only a small number of policy options.

Implications for the neoliberal economic philosophy

Basel 3 was conceived in a wider context characterised by major failures in the banking and financial sectors. As a result, unravelling events 'created a sense of urgency for policy-makers and politicians to be seen to be doing something in order to respond to rapidly unfolding events by taking affirmative action' (Baker, 2015:353). There therefore existed both an imperative and pressure to be seen to be taking immediate action.

These calls seemingly gave rise to an inter-subjectively-held consensus among actors constituting the coordinative discourse that under-regulated, under-supervised and under-capitalised banks were major precipitating causes of a banking and financial sector collapse that contributed to the worst economic downturn since the Great Depression. Therefore, regulatory reforms were highlighted by prominent senior officials in the IMF, along with those in the G20/FSB as an area requiring overhaul (Blanchard, 2009, 2010; G20, 2008a, 2009, 2009a; Strauss-Kahn, 2008a, 2009; Vinals, 2009).

However, an assumption is made here that, despite allusions to the contrary during the second phase the IMF never abandoned its normative commitment to the neoliberal economic philosophy and what it considered the appropriate role of states and markets in the management of the financial sector. This had important implications for the regulatory reform agenda, particularly Basel 3, which was from its earliest inception, limited in its scope by existing economic orthodoxy. Indeed, the preceding discussion shows how the manner in which the IMF approached the regulatory reform agenda was bounded by the confines of the broader neoliberal discourse.

As a result, it is postulated that the Basel 3 reforms advocated during the second phase can be more accurately described as being more about managing failure in the banking and financial systems. That is, there was no desire on the part of the IMF and others constituting the coordinative discourse to significantly alter the existing regulatory and supervisory framework. Rather, an attempt was made to protect neoliberalism from its follies as opposed to attempt to significantly reorient prevailing economic ideas.

This is demonstrable in the previous chapter which observed that, as the second phase of the downturn unfolded, there developed an emerging discourse around the necessity for the construction of a new set of capital requirements that would supersede Basel 2. At this juncture multiple opportunities for alternative forms of economic coordination were possible. As part of the process of selection, a range of actors might be expected to engage in the conceptualization of appropriate solutions, with each identifying the causes of failure and guiding policymakers of the appropriate means by which to resolve them.

These are termed "discursive struggles" (Schmidt, 2013:5) in which actors establish problem definitions, define ideas, and create shared meanings on which policymakers act. Here the notion of authority is key as faced with conflicting opinions, politicians decide who to regard as authoritative, especially on matters of technical complexity including banking reform.

In this particular instance, G20 leaders tasked a particular set of global economic governance institutions (IMF/FSF/BIS) with conceptualising the downturn and coordinating appropriate responses. These institutions however had played a crucial part in developing and seeking to entrench the market-friendly approach to banking and financial sector regulation and supervision that characterised the period preceding the downturn.

Moreover, there was nothing to suggest that they had broken with economic orthodoxy in light of events. Rather, an assumption is made here that they continued to exhibit an inter-subjectively held belief in the efficacy of the prevailing neoliberal economic philosophy, problem definitions, and policy priorities. Crucially, these economic ideas were not simply the aggregation of the beliefs held by each institution which, by coincidence, happened to experience and interpret the political-economy in a like-wise fashion. Rather, their adherence to neoliberal economic ideas ‘exist as collective knowledge’, persisting ‘beyond the lives of individual social actors’, helping to define their social reality (Adler, 1997:327).

As a result, a political decision was made that essentially limited the discourse in which discussion of the potential for alternatives took place by bounding the range of possible solutions and responses. Indeed, Tsingou (2010:21) noted that although there appeared to be a considerable degree of consensus regarding the direction of regulatory reform during the second phase of the downturn, much of the agenda ‘continued to be formulated by the same policy community of experts, operating in the same institutions... who were given the responsibility to see us through the crisis and its aftermath’ (Baker, 2015:340; Kessler, 2012).

Best (2010:39-40) likewise observed a large degree of consistency among such institutions who were ‘on the same page’ on global regulatory reform. Governance arrangements in place prior therefore continued to ‘significantly affect the scope, as well as the intellectual and institutional parameters of international regulatory change’ (Tsingou, 2010:22).

Indeed, Zimmermann (2010:171) observed that although signs suggested that the previous regulatory consensus was cracking, a shift was unlikely as elites that dominated rule-making prior continued to be the most important actors in developing responses. Most pertinently, it is suggested that these institutions - despite the cognitive falsification of key economic ideas underpinning regulatory standards - continued to exhibit a normative commitment to the neoliberal economic philosophy which made explicit assumptions about the extent to which financial markets should or should not be subjected to state intervention and regulation.

This shows how the manner in which the IMF responded to the second phase of the down-turn continued to be framed within the broader ‘discursive fields’ (Steinberg, 1998:856) which the IMF, among other actors constituting the coordinative discourse, drew upon to diagnose and respond thereby delimiting the appropriate course of action. As a result, we can see how events continued to be interpreted, even during the most acute phase, through the intellectual frames of reference provided by existing neoliberal economic ideas.

This was demonstrable for example at the G20s Declaration at the November 2008 Washington Summit which noted that although ‘we must lay the foundations for reform to help to ensure that a global crisis such as this one does not happen again’, this was couched within a broader context in which it was observed that ‘our work will be guided by a shared belief that market principles... foster the dynamism, innovation, and entrepreneurship that are essential for economic growth (G20, 2008a:1). Indeed, adherence to these principles, it was suggested, had significantly raised the global standard of living, lifting millions of people out of poverty in the process.

Against this backdrop, the G20 (2008:3) noted that ‘we will make regulatory regimes more effective over the economic cycle, while ensuring that regulation is efficient, does not stifle innovation, and encourages expanded trade in financial products and services’. This was a sentiment echoed at the September 2009 Pittsburgh Summit which although highlighting ‘there are different approaches to economic development and prosperity, and the strategies to achieve these goals may vary according to countries’ circumstances’, this was couched in an assumption that countries would continue to ‘support open markets, foster fair and transparent competition, and promote entrepreneurship and innovation’ (G20, 2009a:20).

Similarly, in questioning what relevance the lessons of the downturn had for the financial sector, it is worth quoting at length Strauss-Kahn (2009d: 5) who suggested that ‘it would be tempting to conclude that the “modern” financial model should be consigned to the dust heap of history – and that therefore, financial development should be halted. But this would be the wrong conclusion. By enabling banks and capital markets to match up savers and investors – both within and across countries – ever more efficiently, financial development has played a vital role in supporting economic growth. It should be allowed to continue to play this dynamic role – though of course within a framework that controls excess risk, at the same time that it rewards innovation and effort’. These comments therefore suggested that, even during its most acute phase, the G20 and IMF had not completely abandoned their commitment to the neoliberal economic philosophy.

As a result, within this narrowly constituted discourse, the IMF, and others, deferred to existing neoliberal economic ideas and their established intellectual language that specified approved terms of reference. Using these restricted what was thought plausible in reform discussions, thereby specifying the parameters of what was practical for politicians and policy-makers. As a result, the theoretical frames in place prior helped define not only the downturn, but the vocabularies through which its possible solutions were narrated. This ensured that institutions constructing the coordinative discourse were talking about the same thing at the same level, thereby defining a very limited space of communication.

In deferring once again to the perceived efficacy of the neoliberal economic philosophy, problem definitions and policy priorities, we can see how the IMF, along with other actors in the coordinative discourse, sought to reassert prior neoliberal economic ideas. Steinberg (1998:854) is useful here in drawing our attention to the fact that every social order is characterised by a particular set of ideas, in this instance, neoliberal economic ideas, that privilege some stylizations over others, that is characterised by a particular vocabulary that limits the scope of reasonable discussion, meanings, and provides a lens for interpretation.

With this in mind, we can see how the IMF sought to once again stabilize the flow of meanings for communication. That is, discourse was once again characterised by the need for restraint in the capital adequacy debate, the downside to too-stringent regulation, along with the need not to impede too much the functioning of free markets. This discourse once again provided the means by which the IMF, along with the FSB and BIS, attempted to define the common sense along with their meanings for policymakers (Steinberg, 1998:854).

Doing so however silenced and marginalised groups not adhering to the dominant discourse and participating in a community constituted by common knowledge and understandings of the basic functioning of the economy. This lack of deliberation of potential, more radical alternatives, however, prevented politicians, regulators and supervisors from acquiring the kind of critical analysis that would enable them to appropriately distinguish between reform ideas in keeping with the interests of their affected citizenries and those that were not.

That this was the case shows how knowledge claims, in this case even those seemingly discredited during the downturn, had become so indelibly entrenched that they were normalised as ‘institutional facts’ (Searle, 1995). These ‘facts’ were nevertheless subsequently drawn upon to ensure that, even during the most acute phase of the down-turn, prior assumptions were not evacuated. Indeed, these concepts helped to stabilize through minimal tinkering, rather than provide scope for, significant regulatory reforms.

This goes a long way towards explaining why the bulk of reform proposals did not push for a more substantive overhaul of existing regulatory practices but was, in the end, more about making minor adjustments within a broader context that, despite the severity of the downturn, nevertheless continued to be considered as being relatively stable. As a result, rather than wholesale changes, the opportunity for a significant turning point in financial regulation was never fully explored by policymakers.

Indeed, Porter (2010:57) suggested that a striking feature of reform was the degree to which changes were only incremental, ‘building on existing practices rather than initiating or signalling dramatic alterations in governance’. As a result, ‘the key terms of the explicit contract between finance and the state remain unchallenged and the special role of the financial sector was, if anything, reinforced’ (Tsingou, 2010:22). Similarly, Baker (2015:343) noted that ‘many pre-crash beliefs remain prominent’ characterised by ‘evidence of ideational stickiness and inertia’ which meant that ‘despite some policy experimentation, overarching policy frameworks and their rationales have not as yet been overhauled’.

Against this backdrop, although the suggested potential for a ‘new financial architecture’ Strauss-Kahn (2009d:5) had seemingly provided a permissive context in which policymakers and practitioners would be afforded the opportunity to ‘think imaginatively and act boldly’ (Strauss-Kahn, 2008c:6), the continuing normative commitment of the IMF and other actors of the coordinative discourse to the neoliberal economic philosophy meant reforms were, in the end, neither bold nor imaginative.

The direction for reform advocated in the coordinative discourse can therefore in fact be considered as being representative of the paradoxical product of the common adherence to inter-subjectively held neoliberal economic ideas centred around normative assumptions regarding the efficacy of the market. This suggests that the regulatory reform debate was guided, and ultimately limited by, knowledge-based experts within the IMF, FSB and BIS who all continued to be ‘guided by a distinctly neoliberal logic’ (Major, 2012:537).

That the scope for regulatory reforms were severely limited by prevailing institutions and their attendant economic ideas therefore suggests that the process of change is not as benign as that postulated by Schmidt (2010, 2011) who - drawing on the concepts of discursive and deliberative democracy - suggests that ideas developed in the coordinative discourse are subject to deliberation and contestation. Rather, in this case the technical specifications of financial regulation were effectively articulated in opaque sub-committees operating in the absence of due process, with an advantage bestowed on actors best informed about the policy agenda - large financial institutions with close links to the regulatory community.

This meant that, despite the huge political consequences of the downturn, discussion of, and the intricacies of, international financial regulatory policy reform were effectively articulated by technocratic experts devoid of political oversight who were more interested in ensuring the continuity of an existing set of economic ideas and associated policies.

Policy implications

So far it has been suggested that the IMF entered the third phase of the downturn having not abandoned its normative commitment to the neoliberal economic philosophy. This had important implications for the manner in which economic problems were framed; that is, a shift from support for major regulatory reform to calls for caution in the reform agenda.

What therefore, can this tell us about the policy realm, in particular Basel 3 which was described by Strauss-Kahn (2010) as 'a major step to fundamental regulatory reform'? The answer is simple. Given that Basel 3 was conceived through a narrowly circumscribed neoliberal economic philosophy, despite suggestions to the contrary, reforms were not as comprehensive or imaginative as suggested. Paradoxically, this is demonstrable in the two areas that the IMF has held up as a cornerstone of Basel 3: the quantity and quality of capital; and its key macro-prudential component, the counter-cyclical buffer.

Quantity and quality of capital

In the case of the quantity and quality of capital, the notion of extra capital was considered paramount, being as it was, assumed capable of absorbing large losses in the event of an economic downturn. Indeed, Basel 3 operated on the assumption that if a well capitalised bank got into trouble, its shareholders would suffer, but depositors and the taxpayers who insure the deposits, and the rest of the financial system, would be protected. Nevertheless, the editors of Bloomberg (2012:1), in a special Editorial, noted that although equity of 7 percent constituted an improvement over Basel 2, it was still far less than was necessary.

In a similar vein, Admati (2013:2) observed that regulatory changes would allow banks to fund up to 97 percent of their assets with borrowed money with some investments having the potential to be made entirely by borrowed funds. As a result, Basel 3 continued to set insufficient capital requirements, and in doing so, maintained a failed approach to adjusting the requirements to risk. Indeed, the prevailing consensus, perhaps nowhere more evident than in the IMF based on the preceding research, was that 'regulations everywhere appear to be based on the false notion that banks should have "just enough" equity' (Admati, 2013:2), as opposed to instead seeking to force banks' investors to bear more of their own risk, and thereby care about managing it more effectively.

Helleiner (2014:107-108) similarly noted that although minimum capital ratios were set higher than before the downturn, they were still only as high as the ratios held by many financial institutions that found themselves in grave danger during its most acute phase. As a result, there existed the potential for banks operating under Basel 3 to end with capital requirements no higher than Lehman's the day before it failed.

Indeed, the Chairman of the FSB noted in a report to the G20 that many large internationally active banks were on course to meet Basel 3 capital requirements almost five years in advance of the deadline (FSB, 2014:2). The reason for doing so might simply be that banks have taken on board the need for reform and have implemented regulatory changes sooner rather than later. The more likely scenario however is that capital requirements were set at such a low that they were readily implementable in a very short time-frame.

Furthermore, Helleiner (2014:107-108) argues that Basel 3 has been heavily criticised for allowing banks to continue to use internal models for risk weighting of assets. However, this was one of the most "market-friendly" features of Basel 2, the consequences of which were revealed starkly by the downturn. Therefore, the risk of banks using models that deliberately lowered their capital requirements endured after the downturn. Indeed, a study commissioned by the BCBS in early 2013 showed enormous variations in capital held against the same assets by different banks because of assumptions made in models. This led some regulators to worry that banks were continuing to distort the intention of the rules in much the same manner that they had done under Basel 2.

Policymakers were therefore shown to have been very timid in their handling of the manner in which risks are assessed, electing to maintain significant proportions of some of the most dangerous aspects of Basel 2 'with the new Basel 3 rules taking only a baby step toward real change' (Rogoff, 2012:2). As a result, elegant models continue to be defended, in spite of the fact that the downturn demonstrated that were in fact deeply flawed models of perfect markets that created an illusion of safety for a system that is highly risk prone.

The editors of Bloomberg (2012:2) similarly observed that even under the new regime, some supposedly risk-free assets would continue to require little or no capital backing. Indeed, Basel 3 sets a floor of just 3 percent for equity as a proportion of total assets whereas in fact a much higher figure – as high as 20 percent of assets according to the authors – was required, although the consensus seems to be to recoil in horror at such a suggestion. Indeed, so dissatisfied were the authors with Basel 3, they suggested the need for regulators to start from scratch in order to develop much more stringent standards.

Taken together therefore, it would not be without merit to suggest that in spite of the massive de-legitimisation that has taken place as a result of the downturn, the IMF has, along with other global economic governance institutions and private actors, limited the degree of regulatory constraint to which financial institutions have been subject. That is, rather than seek to overhaul the international regulatory architecture as it seemed there was a considerable degree of recognition/approval of the need to do, the IMF, FSB, BIS and others appear happy to set only the most minimum of standards and ultimately leave it to national policymakers and regulators to implement according to domestic constraints.

What is especially remarkable about the continuity observed here, according to Morgan (2011), 'is that all this has happened within three years of a massive financial crash… where banks are extremely unpopular. Nevertheless, those motivated by continuity were able to retain some key parts of the business model which contributed to all this. In spite of all the contestation, law has been reshaped only to a minimal extent and the power of financial institutions, despite its weakening in the aftermath of the crash, has been reasserted'.

The counter-cyclical buffer

In addition to the preceding critique, Shin (2010:1) has questioned the efficacy of the macro-prudential aspect of Basel 3, the counter-cyclical capital buffer, noting that it is 'is almost exclusively micro-prudential in its focus, concerned with the solvency of individual banks, rather than being macro-prudential, concerned with the resilience of the financial system as a whole'. Here, Shin notes the repeated references to greater "loss absorbency" of bank capital, suggesting that this is almost certainly inadequate in achieving a stable financial system for two reasons.

Firstly, Shin (2010:1) suggests that loss absorbency does not address directly excessive asset growth during booms. That is, during a boom, high bank profitability and low risks bolster bank capital ratios. However, experience shows that rapid loan growth is achieved only at the expense of lowering lending standards. This calls into question the philosophy of relying on capital ratios while neglecting the importance of asset growth. Indeed, Shin suggests that although larger capital cushions would have mitigated the shock to the real economy, the experience of countries such as Spain suggests that forward-looking provisioning may not be sufficient and that other tools (such as caps on loan-to-value ratios) become increasingly important.

Secondly, preoccupation with loss absorbency diverts attention from the liabilities side of banks' balance sheets. Here, excessive asset growth is mirrored on the liabilities side of the balance sheet by shifts in the composition of bank funding. The core funding available to the banking sector is retail deposits of household savers. In a lending boom, when credit grows rapidly, the pool of retail deposits is not sufficient to fund the increase in bank credit and other sources of funding are tapped to further fund lending. As a result, the proportion of non-core liabilities of banks serves as a useful indicator of the stage of the financial cycle and the degree of vulnerability of the banking system to a downturn of the financial cycle. Taken together, an assumption is made that these are closely related to systemic risk and interconnectedness between banks, yet addressing them would go a long way towards mitigating systemic risks and the cross-exposure across banks.

Offering an alternative line of critique, Repullo and Saurina (2011:3) suggest that a key element of the proposal was to identify a macro-economic variable or group of variables in order to assess the extent to which in any given jurisdiction there was a significant risk that credit had grown to excessive levels. For each jurisdiction, when the variable breached pre-defined thresholds this would give rise to a benchmark buffer requirement. This could then be used by national jurisdictions to expand the size of the capital conservation buffer. This, however, was problematic for two reasons.

First was the variable its self. An IMF/FSB/BIS Progress Report (2011:5-6) found countries were deploying a range of measures to assess systemic risks, including: aggregate indicators of imbalances drawing on macro-economic or balance-sheet data to signal the build-up of risks in the financial system and broader economy; indicators of market conditions which may lead to generalised distress such as spreads; and metrics of concentration of risk within the system which look at the potential channels of contagion and amplification.

That various measures prevail is consistent with the assumption that optimal choices ought to be country and context specific. What this does do however, is render problematic the claim made in the Report (2011:19) that cooperation on macro-prudential policies requires ‘strong institutional mechanisms to promote a common understanding of threats to global financial stability and adequate policy actions’, along with associated ‘steps to ensure that macro-prudential frameworks in individual countries are mutually consistent’.

Secondly, the countercyclical buffer was considered the most significant macro-prudential component of Basel 3. However that it was not part of a rules-based regime draws attention to the fact that the implementation of one of the most innovative features of Basel 3 was again left open to potential circumvention as the implementation of rules were deliberately left to the discretion of national authorities (Helleiner, 2014:12). So for example, a key assumption was that it was authorities themselves who would advocate the release of the counter-cyclical capital buffer ‘based on incipient signs of strains’ (IMF/FSB/BIS, 2011:13).

If reaching common agreement on an appropriate variable has proven difficult however, then so too is ascertaining the point at which that variable suggests the need for policy intervention, which is its self an inherently subjective exercise dependent on a range of domestic political economy constraints and considerations. Indeed, it has been shown throughout this research that purportedly material 'facts' of the political-economy come with no obvious metric, and that events and their associated implications, are inherently contested. Similarly, in this particular instance, it is ‘in both the build-up and release phase of the buffer' that 'the exercise of judgement remains critical’ (IMF/FSB/BIS, 2011:13).

That this is the case domestically implies that reaching agreement internationally on timing, given the collection of political economies, becomes all the more difficult. Certainly, the deliberative process of when to release buffers is influenced, and therefore complicated by, the fact that this judgement process may create an uneven playing field at the international level, thereby making decision-makers slow to act on signals. Indeed, Keynes reminds us that markets are subject to shifts in sentiment and may react negatively to a decision to release the buffer in worsening economic conditions. As a result, many analysts were left wondering whether authorities would be willing to take the unpopular decision to raise capital requirements during boom times in ways that might curtail lending and reduce comparative advantages vis-a-vis countries electing not to do so (Helleiner, 2014:107-108).

Moreover, further potential sources of tension were observed in the Progress Report (2011:18) regards when to release counter-cyclical buffers down to reduce impediments to the flow of credit to the economy. Banking supervisors, generally oriented towards a MicPR approach, would prefer to keep the increased capital buffer to guard against heightened risks to individual financial institutions. Although it is clear that under such circumstances it is important to assign a clear demarcation of decision-making responsibilities, it is not clear how this relationship might actually function once established, how such tensions might be resolved, and what explicit mechanisms might be available to resolve this process.

Basel 3 as a series of technical fixes

The preceding discussion suggests there was no significant reform of financial regulation. Rather, the fundamental structure of the banking industry was unchanged and regulatory institutions were not significantly strengthened. In fact, although the edifice created in the preceding few decades has needed shoring up with vast quantities of taxpayer money, surprisingly, very little at all has been given in return (Wilson & Grant, 2011:249).

In 2009 MCMD Director Jose Vinals questioned whether there was a need to throw out the old rule books for financial regulation, or whether it would be sufficient to change a few pages and add a couple of chapters. This chapter suggests it is the latter that has played out.

As a result, reforms were clearly not as bold and imaginative as were initially envisaged because none of the proposals, including Basel 3, involved major regulatory change. Rather, drawing on the work of Best (2004:383) we can see how global economic governance institutions have sought to simply manage the failure brought about by banking and financial sector pathologies through the instantiation of a series of ‘technical fixes’ to an already-existing set of policies which were themselves initially conceived in an architecture of global economic governance characterised by an inherently neoliberal political economy.

As a result, eight years after the onset of the downturn, the content of global regulatory reforms are left looking remarkably tame in comparison to the predictions advanced, and promises made, in 2008. Indeed, rather than overturning the market-friendly nature of prior global financial standards, the IMF and others have simply advocated tweaking its content.

Blundell-Wignall and Atkinson (2010:10) of the OECD for example have noted that the aim of Basel 1 was to require banks to maintain enough capital to absorb losses without causing systemic problems as well as to provide a level playing field internationally. A revised Basel framework was introduced in 2004 after a series of concerns with Basel 1, most notable among which was that regulatory arbitrage was rampant and allowed banks to control the amount of capital they required by shifting between on-balance-sheet assets with different weights, and by securitising assets and shifting them off-balance-sheet.

This notwithstanding, the revised Basel 2 retained many of the basic features of Basel 1 which were shown to be wholly inadequate in the context of the current downturn. Similarly, with Basel 3 drawing on many of the assumptions of Basel 2 it is entirely plausible that, just as Basel 2 had proven insufficient, so too did there exist the possibility for Basel 3 to be equally ineffective in its capacity to prevent future downturns of a similar magnitude.

This minimal tinkering suggests the absence of fundamental restructuring of the regulatory architecture of the type proposed during the second phase. Rather, the IMF, and others, can be understood as having adopted a path of expediency through limited reforms. With this in mind, the global financial governance regulatory landscape can, despite the downturn, be characterised as a ‘status quo event’ (Helleiner, 2014:2) for the IMF. That is, despite the fact that there were some changes in the policy realm, the market-friendly character of financial standards, themselves a reflection of the neoliberal economic philosophy, were not significantly overhauled.

This led Admati (2013:1) to suggest that ‘the world’s financial system remains dangerous and dysfunctional’, and perhaps more pertinently, ‘despite years of debate, no consensus about the nature of the financial system’s problems – much less how to fix them – has emerged’. Rather, the regulations in place when the downturn erupted, despite minimal alterations, continue to be inadequate in both their scope and enforcement potential.

Rogoff (2012:1) similarly observed that ‘people often ask if regulators and legislators have fixed the flaws in the financial system that took the world to the brink of a second Great

Depression. The short answer is no'. Although Rogoff (2012:1) suggested that such was the severity of the downturn, investors and regulators would not allow recklessness to hit full throttle for a while, 'little has fundamentally changed' long-term. Rather, regulation simply served as a patch to preserve the status quo as politicians and regulators demonstrated a complete lack of political courage or intellectual conviction to move to an altered system.

Indeed, it has been suggested that 'several years beyond the height of the crisis, the financial reform agenda was still only half-baked at best', with some reforms, despite gesturing in the right direction, 'did not go far enough or have not been implemented fully' (Kodres and Claessens, 2014:31). Indeed, so sparse were reforms that Wilson & Grant (2011:7) observed that 'someone losing contact with events in January 2009 and regaining it in 2011 would have been astonished by the disappearance of critiques of markets, corporate behaviour and weak regulation'.

These points were broadly acknowledged in the October 2012 GFSR which observed that despite some improvements: the structure of intermediation was largely unchanged; the financial system remained overly complex; and the too-big-to-fail issues still unresolved, thereby leaving the financial system vulnerable to risks that prevailed prior to the downturn.

By way of adjudicating what a safer financial system might look like, the GFSR (2012a:76) suggested that most people would envisage a system that: is less complex; in which institutions are more transparent; in which institutions are less dependent on leverage; are better capitalised; can better manage liquidity risk; would encourage all risks to be properly priced. Viewed in such a manner, and judging by its own standards, the financial system could not be characterised as being considerably safer than it was prior to the downturn.

That this was the case however should not have been entirely surprising given the GFSR's somewhat startling admission that the global regulatory reform agenda which the IMF had played a contributory part, had not been driven toward directly altering financial sector structures per se, but rather toward promoting safer behaviour in particular segmented areas, in which emphasis was placed on the shoulders of markets and businesses for delivery.

This was undertaken on the assumption that reforms targeted at raising the costs of riskier activities means one can expect changes by the private sector to lower overall costs and move to more profitable activities. Hence, the response of institutions and investors to new requirements, it was assumed, would produce new and altered structures which would then change the larger financial system and structure.

So for example, capital and liquidity requirements under Basel 3 were aimed at improving banks' resilience and ability to absorb losses. In responding to these requirements however, as well as to changing business conditions, banks, it was suggested, would decide what activities to keep and how to structure their funding and capital profiles. Investors would, in turn, decide how to participate and on what terms, decisions which would produce change, much of which was unpredictable as elements of reform were yet to be finalised, and many yet to be implemented. Alternatively, it could lead to no change at all (GFSR, 2012a:82-83).

This reflected an assertion by Vinals et al (2010:6) that a fundamental principle underlying analysis is that 'the private sector plays an important role – it is not up to regulators to "build" the financial system but to influence its direction by providing appropriate rules and incentives'. In doing so, it was suggested that 'it is ultimately the industry that will translate rules into actual changes in industry practice. For reform initiatives to be successful, regulatory efforts should continue to be directed toward improving the internal operations of financial firms, including their risk management and governance. They should seek to restore the credibility of market discipline in the face of past failures' (Vinals et al, 2010:25).

Concluding remarks

This chapter has suggested that, the apparent shift observed in the previous chapter notwithstanding, regulatory reforms were in fact characterised by a considerable degree of continuity as opposed to change. This was shown to be so for three reasons.

Firstly, by tasking particular institutions and standard-setting bodies with coordinating the international response as they did (the IMF, FSB, and BIS), the potential for discursive battles in which competing conceptions of the downturn and appropriate responses are played out was inherently limited. That is, they all continued to be underpinned by a distinctively neoliberal economic philosophy.

Secondly, the manner in which economic problems were framed shifted from perceived regulatory failures during the second phase of the downturn to calls within the IMF for a more cautionary approach to the capital adequacy debate during its third phase.

Thirdly, the preceding discussion suggests that there were important reasons to suggest that the quantity and quality of capital required under Basel 3 was not predicted to be substantially different from that held by financial institutions prior to the downturn. Moreover, the most important macro-prudential component of Basel 3, the counter-cyclical capital buffer was left to domestic policymakers to decide on both the variable by which to judge risk, and the point at which it would be released, which was an inherently subjective endeavour.

Taken together therefore, despite the potential for a significant shift in the prevailing economic philosophy, 'no such dramatic change has occurred' (Guven, 2012:870). That is, there has been no fundamental divergence from the pre-existing repertoire of problem definition or economic philosophy. Rather, the downturn has in fact been characterised by prescriptive continuity as what may have appeared to have been attitudinal shifts, have yet to trigger fundamental modifications in programme design.

Conclusion

'While it is always possible to wake a person who is sleeping, no amount of noise will wake a person who is pretending to be asleep'
(Jonathan Safran Foer)

In 2008 the world witnessed what has been broadly contextualised as the worst financial and economic downturn since the Great Depression. As opposed to being the result of an exogenous event puncturing an otherwise relatively stable overall economic framework, this research has suggested that, inherent to the downturn, was a fundamental failure of the neoliberal economic ideas steering IMF actions. As a result, we would not be without justification in suggesting that, at a minimum, the consequences would be equally as damaging to dominant economic ideas as the Depression was to liberalism, and the Great Inflation had been to Keynesianism.

In both instances, the failure of existing economic ideas was inter-subjectively interpreted by actors as a crisis which ultimately precipitated a shift to an alternative set of economic ideas characterised by an altogether different economic philosophy, problem definitions, and associated policy priorities. With this in mind, it was widely anticipated that the current downturn had the potential to exert a similarly transformative dynamic.

Against this backdrop, and given the preceding research, we are suitably positioned to revisit, and provide satisfactory answers to the research questions posed in the Introduction, one of which is empirical, and the other theoretical. We begin first of all with the empirical question relating to the extent to which it is possible to talk of change or continuity in neoliberal economic ideas in the IMF.

In answering this question, this research has advanced the simple assertion that economic ideas in the IMF are characterised by continuity as opposed to change. As a result, the downturn can be best described as what Helleiner (2014:3) has termed a 'status quo event' for the IMF.

This finding runs contrary to a number of studies providing an analysis of continuity and change in the IMF. Babb (2011) for example has spoken of 'productive incoherence' (the proliferation of incoherent and/or contradictory statements from the IMF) and an interregnum characterised by new development opportunities, particularly in relation to the gradual normalization of capital controls which ‘may represent the beginning of what may very well turn out to be the most significant expansion of policy space’ over the last few decades (Babb, 2011:807).

In a broadly similar fashion Ban (2014), in questioning whether or not there is increased space to negotiate with the IMF on fiscal policy, suggests that there is, thanks by and large to the ‘Keynesian’ turn in the IMF. Although not citing this as a potential paradigm shift, Ban nevertheless observes the existence of a doctrinal shift in fiscal policy in which it is possible to find more arguments for less austerity, more growth measures, and a fairer social distribution of the burden of fiscal sustainability.

This therefore begs the question of how we account for such differences in interpretation. It is here that this research takes as it point of departure the fact that although economic ideas are often held up as a single concept, they in fact reside at three levels of generality: economic philosophies; problem definitions; and policy priorities.

When understood as such, we are able to distinguish, at one level of generality, the common theme among the preceding studies, that is, an analysis of continuity or change limited to an exploration of the policy realm. In doing so, and given the severity of the downturn, a series of policies were advocated by the IMF that was often experimental, and at times simply contradictory to extant orthodoxy. Consequently, it is not difficult find evidence of discontinuity in a range of policy areas, and therefore, to see why such conclusions were drawn.

Indeed, such studies are consistent with much constructivist literature which draws attention to the fact that it is policies that change most rapidly when windows of opportunity open up in which to enact change. Chapters 4 and 6 of this research may appear, superficially at least, to support this approach by demonstrating how calls for substantial fiscal stimulus along with increased regulation of the banking and financial sectors, prevailed during the most acute phase of the downturn.

Nevertheless, and contrary to such approaches, this research has advocated that the most appropriate means by which to adjudicate between change and continuity is by analysing the impact of the downturn on the underlying economic philosophy held by actors. That is, assumptions made regarding the perceived efficacy of states or markets in the functioning of the economy and accompanying problem definitions.

When altering our level of analysis, we can see how the ostensible change observed by Babb (2011) and Ban (2014) among others, was not in fact as profound as initially envisaged. Indeed, when we delve beyond the policy realm into an exploration of the deeper economic philosophy of the IMF, we see, consistent with Chapters 5 and 7 of this research, how the IMF never in fact abandoned its basic articles of faith, even during the most acute phase of the downturn.

Therefore, although a range of policies advocated during the second phase of the downturn seemingly run contrary to those advocated even months prior, these were clearly not a carefully articulated response to the accumulated pathologies of neoliberal political-economic failure. Rather, they can be more accurately described as failure management techniques, the aims of which were not to significantly alter the neoliberal economic ideas steering IMF actions, but were rather an that attempt to save neoliberalism from its follies.

What followed during the third phase of the downturn can therefore be more accurately interpreted as an attempt by the IMF, having stemmed the most immediate danger, to re-establish the status quo ante. That it interpreted the downturn in such a manner leaves us well placed to talk, with some considerable degree of conviction, of continuity rather than change in economic ideas in the IMF.

This assertion notwithstanding, by focusing on the underlying economic philosophy held by the IMF, and given that these are often held up as the slowest and most resistant to change, there exists the potential for assuming that because nothing fundamental has changed, that nothing at all has changed. This is not the case as there has been some modicum of change, notwithstanding the fact that this has remained limited to the policy realm. However, this does not entirely preclude the potential for future, more substantive change in economic philosophy and problem definitions in the IMF. This is so for two reasons.

Potential sources of change

Top-down

Gamble (2014) and Payne (2014) have drawn attention to the fact that transformations in what have been referred to here as economic philosophies and problem definitions typically take much longer to play out than is generally conceived, often in the order of fifteen years. Indeed, in the policy areas explored in this research, debate within the IMF, and beyond, is still very much a work in progress.

On the one hand, of economic policy, discussion remains regarding the appropriate form and function of monetary policy. Namely, the extent to which central banks should, or should not attempt to counter asset bubbles (a re-emergence of the lean versus clean debate), and whether it should target a higher rate of inflation to give more flexibility to prevent rates quickly hitting the ZLB. Moreover, discussion remains on UMPs, particularly with reference to forward guidance on the policy rate, and whether they might become a more significant part of the future policy mix (IMF, 2013b).

On the other hand, the regulatory reform agenda remains incomplete, with the IMF continuing to engage in discussions regarding reforms in a number of areas not subject to discussion in this research. These relate for example, to the regulation of the shadow banking system including hedge funds, the need to better regulate the markets for securities and derivatives, and the need to address the too-important -to-fail problem. Taken together, these areas might eventually alter the direction of the economic ideas steering the course of global economic governance in such a manner that it may become possible to talk of change as opposed to continuity (see for example Vinals, 2014:1).

Bottom-up

Moreover, the focus of this research has been on elite-elite interactions in the coordinative discourse and how economic ideas and accompanying policy priorities are subsequently diffused through the communicative discourse. However, in contrast to these 'top-down' considerations it is not inconceivable that an alternative means by which change might yet come about is ‘bottom-up’. Here, although little may have currently changed in the IMF the potential exists for the neoliberal economic philosophy and problem definitions to fail to sufficiently address low growth, stubbornly high rates of unemployment, and in some instances, prolonged periods of austerity.

Indeed, Schmidt (2008:308) draws our attention to the fact that the use of the philosophy of science can only go so far as whereas in science 'programmatic success is judged by scientists alone; in society, programmatic success is judged not only by social scientists but also by citizens'. Indeed, in a similar vein, Widmaier et al (2007:755) remind us that everyday politics can matter more than elite debates.

As a result, the success of a particular set of policies does not simply depend on the presence of cognitive ideas capable of satisfying policymakers that a given programme will provide robust solutions. 'It also depends on the presence of complementary normative ideas capable of satisfying policymakers *and citizens alike that those solutions also serve the underlying values of the polity'* (Schmidt, 2008:308, emphasis added).

Nevertheless, elite ideas regarding the need for a particular course of action has the potential to clash with ideas about economic justice. It is therefore not inconceivable that elites fail in their ability to legitimise or naturalise the kind of arguments deployed in this research to successfully justify the efficacy of continuity.

As a result, the fall-out from the downturn could yet lead a disaffected citizenry to seek an alternative political-economy to that provided by adherence to neoliberal economic ideas. Doing so may eventually contribute to changed perceptions regarding the relative efficacy of states and markets, the manner in which economic problems are interpreted and responded to, and therefore the kinds of policies considered both necessary and desirable from a social perspective.

Continuity in neoliberal economic ideas as contributing to a potentially irrelevant IMF

The preceding discussion suggests that there still exists the potential for change to be brought about by the downturn, and thereby an alternative political economy that envisages a privileged role for the state in the functioning of the economy. Moreover however, there are also important implications, and potential challenges to, the IMF if it elects to maintain its doctrinaire adherence to neoliberal economic ideas.

Indeed, should we accept Skidelsky's (2010:xvi) assertion that it is difficult to convey the harm done by the recent downturn to neoliberal economic ideas, yet the IMF chooses to do nothing in the face of such monumental falsification, its unwavering commitment to existing economic orthodoxy might yet result in an increasingly irrelevant IMF.

Indeed, running parallel to, and further exacerbating this potential are broader structural changes taking place in the international political economy. Prior to the downturn the relevance of the IMF appeared to have diminished significantly. With only a limited number of loans outstanding the IMF, for example, was labelled the "Turkish Monetary Fund" on reflection of Turkey's position as main debtor country (Drezner, 2014:8). Additionally, the IMF had undergone a period of scaling back its activities, with much of its gold being sold, and a large number of staff cuts that had either been, or were due to be, implemented.

Countries only approach the IMF for assistance during moments of political-economic failure. Given the relatively benign economic environment that characterised much of the global economy prior to the downturn, it might not be entirely inaccurate to suggest that this was the primary reason for the IMFs diminishing loan portfolio.

What was happening however was arguably much more fundamental. It was not that developing countries were not borrowing. It is that they were not borrowing from the IMF. Indeed, many countries, acutely aware of the doctrinaire approach of the IMF were reluctant to access loans accompanied by stringent conditionality.

The problem therefore exists, given the IMF's continuing deference to neoliberal economic ideas, that despite their clear cognitive and normative falsification, and despite increasing its lending substantially during the current downturn, for the real potential for it to find its self in a similar, if not more isolated position, than it occupied prior to the downturn.

In light of this potential, at its Washington summit the G20 group of state leaders stated that they were 'committed to advancing the reform of the Bretton Woods Institutions so that they can more adequately reflect changing economic weights in the world economy in order to increase their legitimacy and effectiveness' (G20, 2008a:4), by giving developing economies a greater voice and representation (see also G20, 2009a:3; G20, 2010:5).

These calls notwithstanding, change has simply not been forthcoming (IMF, 2015:1-3). Indeed, in consistently failing to act on reforms, Lombardi (2014) has suggested that the IMF, and in particular the US, had broken the implicit contract underpinning G20 and IMF commitments to giving a greater voice to developing countries.

The result, according to Lombardi (2014) is that the failure to implement reforms would give momentum to regional alternatives, thereby leading developing countries to look elsewhere for financial assistance. Similarly, the Economist (2014) has noted that delays in reforms have left a number of countries impatient for change, thereby leading them to take matters into their own hands, further contributing to the potential marginalization of the IMF.

Indeed, partly in response to the inability of the IMF to make progress on quota reforms this is exactly what has been happening. China has helped create the Asia Infrastructure Investment Bank (AIIB) which a number of commentators suggest has been set up in response to the lack of substantive reform in the IMF (see for example Sands, 2015).

Similarly, the BRICS group of countries (Brazil, Russia, India, China and South Africa) have created the New Development Bank (NDB) which has stated explicitly that it operates 'as an alternative to the US-dominated World Bank and International Monetary Fund' (NDB, 2015). Regardless of if, or which, of the preceding scenarios may eventually bear substantive fruition, we can nevertheless conclude that, in the absence of change in the IMF, there exists a real potential of it becoming an increasingly irrelevant monetary fund.

The preceding discussion certainly raises a great many more questions than this research has answered, thereby suggesting the existence of considerable scope for further enquiry in this area. Despite the focus on the policy areas discussed in this research, arguably the most pertinent concerns the potential challenges to the IMF such as the creation of regional lending bodies and the creation of the New Development Bank created by the BRICS in particular.

There are clearly no concrete guarantees at this juncture what the NDBs lending capacity might be, which countries might elect to borrow money, for what purposes, and crucially on what terms. All of these represent interesting avenues of inquiry.

Crucial however are broader issues related to what has been termed here as the coordinative discourse, that is, the apex policy forums or state leaders steering the broad direction of the NDB. Questions arise as to how these key states would be ordered in terms of a hierarchy, implicit or otherwise, and what potential exists for tensions or biases as a result?

Moreover, and just as important are questions related to the economic ideas steering the course of policy action. Namely, does such a grouping of what is an inherently eclectic mix of states with regards both their polities and economies actually exhibit a distinct political-economy characterised by a coherent underlying economic philosophy, problem definitions and policy priorities? If yes, then the question is what do they look like, and in what ways do such economic ideas 'hang together' in such a manner as to steer policy actions.

Constructing continuity in economic ideas in the IMF

Given the foregoing discussion, we can now revisit and provide satisfactory answers to the theoretical, and second, of the research questions posed in the Introduction: that is, why did the monumental failure of neoliberal economic ideas not result in altered structures (change)?

The starting point for discussion is that, what has been referred to here as the second phase of the downturn, appeared to provide the necessary preconditions (the moment of political-economic failure) for a crisis narrative in which events were inter-subjectively interpreted by agents as requiring decisive intervention (change).

Consistent with much constructivist work, it is here that windows of opportunity open up for the enactment of a range of alternative policies as existing policies, problem definitions and economic philosophies are interpreted by actors as being unable to account for new circumstances. During the current downturn however, not only were a range of policies deployed that had previously been off the table only months prior, but they also appeared to carry with them important implications for the manner in which the relative efficacy of states as opposed to markets were once again understood in the IMF.

Nevertheless, this research has demonstrated how change was ultimately not forthcoming. In addition to accounting for why, a key task has been to take up the challenge by Schmidt (2011:111) 'to provide less deterministic and more dynamic ways of thinking about continuity'.

In doing so, it is suggested that, during times of political-economic uncertainty, agents' interests are radically open. At this juncture it has been suggested that persuasive practices come to the fore, with agents engaging in discursive battles over attempts to successfully interpret, define, and thereby frame the direction of action. Crucially however, this research has suggested that not only are agents motivated by change involved in this process, but so too are those motivated by continuity, and there is no logical reason to suggest that those motivated by change will be victorious.

While this is almost self-evident, what is missing from existing constructivist literature is an adequate understanding of the mechanisms by which actors undertake such an endeavour. As a result, a key contribution of this research has been to demonstrate how agents seek to construct continuity by persuading others of the efficacy of continuing adherence to existing economic ideas. Here we revisit the two concepts developed in this research, historical analogy and the politics of framing.

Historical analogy

On the one hand, this research has sought, drawing on the International Relations literature associated with foreign policy analysis, to posit the efficacy of the import of reasoning through historical analogy - a tool, implicitly or otherwise, used by actors in an attempt to reduce moments of political-economic uncertainty by postulating the broader environment as one of continuing risk - to the study of IPE.

More specifically however, in addition to seeking to advance constructivist IPE generally, this research contributes towards one of the multiple 'pathways' to constructivism postulated by Abdelal et al (2010:10), in this particular instance, the path of cognition. This is an area of study typically associated with psychologists and cultural sociologists who 'have long argued that human beings depend on heuristics and shortcuts to organize action and choice' (Abdelal et al, 2010:10).

Nevertheless, it has been suggested here that historical analogy has the potential to play an especially important role in the study of IPE precisely because the international political economy is often held up as an arena characterised by a considerable degree of complexity, unpredictability and uncertainty rather than risk, a situation which is in principle calculable, and whose outcomes are quasi-normally distributed. Situations of uncertainty however suggest that past events are not necessarily a reliable guide to future probabilities, and it is these moments that are understood as a fundamental part of the contemporary political-economy (Knight, 1958; Taleb & Pipel, 2004). As a result, actors 'filter information from the environment via heuristics and biases and consider it in highly selective ways' (Abdelal et al, 2010:10).

The novelty and utility of the introduction of schemas and historical analogy to this research however, is that it shows precisely how agents attempt to reduce uncertainty during such moments (political-economic failure) in order to construct continuity and stability rather than change.

Indeed, it has been suggested by a number of constructivists (see for example Blyth, 1997, 2002; Hay, 1995, 1999; Widmaier et al, 2007) that during such moments, agents are unsure of their interests, thereby leaving them open to persuasion that one particular course of action over a range of available alternatives, is consistent with their interests.

It is here that, drawing on the concept of schema and historical analogy allow us to better understand how actors react to moments of political-economic failure and associated uncertainty. That is, they provide answers to the preliminary questions: how can we best explain the causes of our current predicament? And thereafter, what are the implications for it being defined as event A over event B?

It is here that drawing on the notion of a 'knowledge structure' allows us to demonstrate how actors assimilate incoming information through existing schemas. This provides them with a means by which to interpret, and thereby make sense of, the vast amounts of incoming information.

This leaves actors well placed to provide a definition of events and occurrences and, in doing so, shows how they do not unambiguously and automatically telegraph to agents their nature and appropriate remedies. Rather, they are differentially experienced and interpreted by actors, a reflection of their underlying economic philosophies and problem definitions.

Moreover, by assimilating this information through the lens provided by existing schemas actors have been shown in this research to reason through historical analogy in order to present events as analogous to others, thereby making the political-economic environment knowable and more closely resembling a situation of risk as opposed to uncertainty. Indeed, accepting this premise, we can see how 'when information about the environment is complex and poses a high level of uncertainty... argumentation by reference to history is a vital component' precisely because it 'serves as a means of persuading both self and others' (Vertzberger, 1986:229).

There are clear implications to reasoning through historical analogy and defining events in one particular manner as opposed to all of the available alternatives. That is, it allows actors to derive policy lessons from past experience which were shown to be successful, and which, particularly for the purpose of this research and consistent with the historical analogy more broadly, are shown to be consistent with existing economic philosophies and problem definitions. Crucially, these are subsequently drawn upon and advocated as tools of persuasion in order to convince other actors of their efficacy.

Framing

Benford and Snow (2000:611) have observed that 'the concept of frame has considerable currency in social sciences today'. This is especially so of the sociology literature and social movement theory in particular, where such approaches have sought to draw attention to the importance of the politics of framing as a means by which to assign meaning to events and occurrences. Nevertheless, making explicit its relevance and insights to the study of constructivist IPE has eluded those working within this approach so far. Yet the suggestion here is that given the complex nature of the international political economy, such a concept has considerable utility.

Against this backdrop, this research contributes to a second pathway to constructivism identified by Abdelal et al (2010:8), the path of meaning, which the authors suggest, 'is the foundation of most explicitly constructivist scholarship'. In doing so, this research builds upon the approach favoured by cognitive constructivists, thereby allowing us to illuminate yet another mechanism by which actors seek to construct continuity.

At base, the concept of framing draws attention to the fact that the opening for socially constructed variation in action is not simply the result of the complexity of the material world, but how these surroundings are viewed in terms of the ideas, identities and symbols, that actors use to frame and prioritize their actions.

Indeed, Abdelal et al (2010:9) suggest that the stronger version of meaning-oriented constructivism draws attention to the fact that actors, rather than interpreting the world around them in purely material terms, endow the political-economy with social purposes which are themselves embedded within a variety of collective identities. This helps us to explain both why some of even the most taken-for-granted assumptions are not entirely uncontested, and why policymakers and market participants discern a variety of meanings from similar events and occurrences.

Should we accept these premises, that the international political economy is indeed uncertain, and characterised by a dynamic context of unpredictability, and that even the least uncertain environment is not free from potential variation in meaning, then we can see how the politics of framing has the potential to constitute an incredibly fruitful means by which to study how actors assign meaning to such events.

In particular however, this research has drawn attention to the important role played by institutions and the performative function they play in their explicit attempts to fix meanings. This is common to much meaning-oriented constructivism which highlights the role of institutions in, for example, defining the "taken-for-granted" status of good governance in development theory in the case of the World Bank (Weaver, 2010:48; see also Barnett and Finnemore, 2004). These show how institutions help to delineate between the acceptable (and in the process, unacceptable) boundaries of what can be considered politically and economically possible (Abdelal et al, 2010:10).

This draws attention to the importance of the economic ideas held by institutions as it is through these that we understand which problems come to be defined and in which particular ways. In essence, economic ideas bring meaning to an event or object and it is to the meaning that they bring to bear to which agents react, not some purported material reality.

Viewed in such a manner, we can see how the process by which meaning is assigned is an inherently political act of strategic social construction on the part of actors inasmuch as it is both deliberate and goal directed (Weaver, 2010:61-64). In contrast to existing meaning-oriented constructivist research however, which makes little or no explicit reference, this research has sought to highlight the utility of the concept of framing. In the process of doing so, it has been show to perform two crucial functions.

Firstly, framing plays a crucial diagnostic function inasmuch as they 'seek to remedy or alter some problematic situation or issue', indeed, 'it follows that directed action is contingent on identification of the source(s) of causality, blame, and/or culpable agents' (Benford & Snow, 2000:616). Understood as such, we can see how assigning meaning is essential as events in the political-economy are not simply obvious to the agents involved.

Secondly, Jobert (1989:382) suggests that whoever is successful in their attempts to impose their interpretation of the problem will have a major influence in the stages that follow. In this regard we can see how framing plays an important prognostic role inasmuch as it involves the articulation of a solution to the problem so-defined, along with a strategy for carrying out that plan. As a result, the prognostic function of framing involves the critical question of what is to be done which is its self heavily influenced and/or constrained by the range of possible solutions and strategies to the problem so-defined.

The preceding discussion notwithstanding, there may at any moment in time be a number of ways of framing a particular event or issue. This begs the question of how we gauge the success, or otherwise, of a particular frame. In answering this question, Chong and

Druckman (2007:109) have observed that 'there is disagreement about the best measure to use to gauge the magnitude of framing effects', but nevertheless suggest that 'one standard is the variance in preferences produced by alternative frames on an issue'. Should we accept this as a suitable metric, then we can see quite clearly that the IMF was indeed successful in framing the third phase of the downturn in such a manner as to construct continuity in economic ideas.

This therefore pushes us to question how the IMF was able to so successfully contribute towards the reduction in the variance of frames, and are there lessons to be learned regarding how actors might successfully frame an event or object. It is here that we find the role of persuasion as being crucial in the process of helping to convince others of the benefits of particular courses of action.

In doing so, this research has shown how the IMF sought to provide cognitive justification for assigning meaning to events, in this particular instance, the need for fiscal adjustment which was premised on technical research which demonstrated the negative consequences associated with excessive sovereign debt burdens. Doing so was an important means by which to validate claims with seemingly apolitical support. Moreover, and equally as important, this was supplemented with normative justification for adjustment. Indeed, it was here that the IMF suggested that many states had lived beyond their means in the period immediately preceding the downturn, and that fiscal retrenchment was a necessary penance to be paid for such profligacy.

Together, this cognitive and normative justification combined to provide a simple yet compelling frame of the third phase of the downturn, and was a critical process by which the IMF sought to convey the efficacy, indeed necessity, of continuing adherence to the neoliberal economic philosophy, problem definitions and policy priorities. Doing so served an important means by which the IMF sought to ensure that the bubbles and frames through which economic problems were interpreted and responded to prior to the downturn did not go away despite its severity.

Just as the empirical question raised the potential for further avenues of enquiry, so can the same principle be applied to our second, theoretical question which has potential benefits and applicability that extends beyond the scope of this research.

First and foremost, a case has been made for a broader application of constructivist IPE as an approach to the international political economy that exceeds a concern with questions of change in the context of crisis, and instead, opens up the potential for a more dynamic understanding of the methods by which actors attempt to affect continuity.

Secondly, these methods, and the theoretical concepts explored here have applicability to a much broader range of empirical contexts than that discussed here. Indeed, when talking of constructing continuity in economic ideas despite their evident falsification, the UK perhaps offers the most strikingly obvious example.

The current downturn has had an enormous impact on the UK given both its disproportionately large financial sector vis-a-vis its competitors, along with its enormous housing bubble that preceded it. Nevertheless, the banking and financial sectors of the UK have not only escaped the downturn largely unscathed, but have if anything emerged, despite calls for a fundamental rebalancing of the economy, to once again being advocated as a key driver of economic growth. Moreover, despite enormous state financed bank bail-outs and other means of economic stimulus, the need for austerity and living within the country's means has emerged, although not entirely uncontested, as the dominant narrative, evidenced by successive Conservative Party election victories.

This raises a number of important questions. On the one hand, what role did existing schemas play in defining the unfolding downturn, and in what way, if at all, were historical analogies drawn upon to reduce the increasing uncertainty? On the other hand how has the downturn, despite its origins being specific to the banking and financial sectors, come to be framed, and therefore diagnosed, as a crisis of the profligate state requiring, according to the accompanying prognosis, an extended period of austerity? And crucially, what were the cognitive and normative arguments made that ultimately created such a successful frame?

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